

United States

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

(Mark One)

☐

REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF
THE SECURITIES EXCHANGE ACT OF 1934

OR

☒

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended: December 31, 2007

OR

☐

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____.

Commission file number: 333-114196

Axtel, S.A.B. de C.V.

(Exact name of Registrant as specified in its charter)

Axtel

(Translation of Registrant's Name into English)

United Mexican States

(Jurisdiction of incorporation or organization)

Blvd. Gustavo Diaz Ordaz 3.33 No. L-1

Col. Unidad San Pedro

San Pedro Garza Garcia, N.L.

Mexico, CP 66215

(Address of principal executive offices)

Securities registered or to be registered pursuant to

Section 12(b) of the Act:

Title of each class

Name of each exchange on which registered

None

Not applicable

Securities registered or to be registered pursuant to Section 12(g) of the Act:

None

(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

(Title of Class)

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report: 96,636,627 Series A and 8,672,716,596 Series B

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes: _____ No: [X]

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes: _____ No: [X]

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days:

Yes: _____ No: [X]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of “accelerated filer and large accelerated filer” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer _____ Accelerated filer _____ Non-accelerated filer [X]

Indicate by check mark which financial statement item the registrant has elected to follow:

Item 17: _____ Item 18: [X]

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes: _____ No: [X]

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Financial Statements	

In this annual report, references to “\$,” “US\$” or “Dollars” are to United States Dollars and references to “Ps.” or “Pesos” are to Mexican Pesos. This annual report contains translations of certain Peso amounts into Dollars at specified rates solely for the convenience of the reader. These translations should not be construed as representations that the Peso amounts actually represent such Dollar amounts or could be converted into Dollars at the rates indicated or at any other rate.

Unless otherwise indicated, this annual report contains discussions and financial information that was prepared in accordance with Mexican financial reporting standards, which we refer to as “Mexican GAAP.” These principles differ in significant respects from U.S. generally accepted accounting principles, which we refer to as “US GAAP,” including, but not limited to, the treatment of the capitalization of pre-operating expenses, the capitalization of interest, severance, and deferred income taxes and employees’ profit sharing and in the presentation of cash flow information.

Forward Looking Statements

This report on Form 20-F contains certain forward-looking statements within the meaning of Section 27A of the United States Securities Act of 1933, as amended, (the “Securities Act”) and Section 21E of the United States Securities Exchange Act of 1934, as amended (the “Exchange Act”). These forward-looking statements reflect our views with respect to our financial performance and future events. All forward-looking statements contained herein are inherently uncertain. Actual results could differ materially from those projected in the forward-looking statements as a result of factors discussed herein. Many of these statements may be identified by the use of forward-looking words such as “believe,” “expect,” “anticipate,” “should,” “planned,” “estimated” and “potential,” among others. Readers are cautioned not to place reliance on these forward-looking statements. The following factors, as well as other factors described in this report, could cause actual results to differ materially from such forward-looking statements:

- competition in local services, long distance, data, internet, voice over internet protocol, or VoIP, services and video;
- ability to attract subscribers;
- changes and developments in technology, including our ability to upgrade our networks to remain competitive and our ability to anticipate and react to frequent and significant technological changes;
- our ability to successfully conclude the integration of Avantel into Axtel;
- our ability to manage, implement and monitor billing and operational support systems;
- an increase in churn, or subscriber cancellations;
- the control of us retained by certain of our stockholders;
- changes in capital availability or cost, including interest rate or foreign currency exchange rate fluctuations;
- our ability to service our debt;
- limitations on our access to sources of financing on competitive terms;
- our need for substantial capital;
- the effects of governmental regulation of the Mexican telecommunications industry;

- declining rates for long distance traffic;
- fluctuations in labor costs;
- foreign currency exchange fluctuations relative to the US dollar or the Mexican peso;
- the general political, economic and competitive conditions in markets and countries where we have operations, including competitive pricing pressures, inflation or deflation and changes in tax rates;
- significant economic or political developments in Mexico and the United States;
- the global telecommunications downturn;
- the timing and occurrence of events which are beyond our control; and
- other factors described in this Form 20-F.

Any forward-looking statements in this Form 20-F are based on certain assumptions and analysis made by us in light of our experience and perception of historical trends, current conditions, expected future developments and other factors we believe are appropriate under the current circumstances. Forward-looking statements are not a guarantee of future performance and actual results or developments may differ materially from expectations. You are therefore cautioned not to place undue reliance on such forward-looking statements. While we continually review trends and uncertainties affecting our results of operations and financial condition, we do not intend to update any particular forward-looking statements contained in this document.

Part I

Item 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

Item 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

Item 3. KEY INFORMATION

A. Selected Financial Data

The following table provides our selected historical consolidated financial data. The selected historical consolidated financial data for the years ended December 31, 2003, 2004, 2005, 2006 and 2007 have been derived from our audited consolidated financial statements included elsewhere in this Form 20-F or in Forms 20-F filed in previous years.

The information presented below should be read in conjunction with “Item 5. Operating and Financial Review and Prospects” and the consolidated financial statements and related notes thereto included elsewhere in this Form 20-F.

Year Ended December 31,				
2003	2004	2005	2006	2007
(Constant Ps. in millions as of December 31, 2007, except ratios, shares and margins)				

Statement of Income Data:

Telephone services and related revenues	3,434.2	4,306.4	5,362.4	6,675.7	12,190.6
Cost of revenues and operating expenses	(3,301.9)	(4,025.0)	(4,716.1)	(5,924.5)	(10,796.8)
Income from operations	132.2	281.4	646.3	751.2	1,393.8
Interest expense, net	(234.0)	(287.1)	(349.9)	(390.6)	(790.6)
Foreign exchange (loss) gain, net	(375.8)	(8.2)	112.1	23.7	1.0
Change in fair value of derivative instruments	—	—	—	(24.8)	19.9
Monetary position	109.2	72.2	58.7	11.5	268.8
Other income (expense), net(1)	2,016.7	23.4	7.7	(32.6)	(20.1)
Cash severance and other items	(12.3)	—	—	—	—
Income before income taxes	1,636.0	81.8	475.0	338.3	872.8
Income tax expense	(580.4)	(167.8)	(167.9)	(117.6)	(383.2)
Equity in results of associated company	—	—	—	1.7	1.4
Net income (loss) from continuing operations	1,055.6	(86.0)	307.1	222.4	491.0
Net income (loss)	1,055.6	(86.0)	307.1	222.4	491.0
Shares outstanding	7,601,120,598	7,601,120,598	8,522,810,598	8,522,810,598	8,769,353,223
Net income (loss) from continuing operations per share (pesos) ...	0.1	(0.0)	0.0	0.0	0.1

Operating Data:

Depreciation and amortization	1,012.3	1,116.6	1,220.3	1,560.1	2,690.7
Investment in property, systems and equipment (fixed assets) (end of period)	730.8	1,629.5	1,767.1	7,854.5	2,486.1
Net Resources:					
Operating activities	377.4	1,239.5	1,524.1	2,532.1	3,226.7
Investing activities	(844.4)	(1,708.4)	(1,825.8)	(8,800.6)	(2,556.4)
Financing activities	1,273.9	(104.3)	1,725.1	5,449.0	(318.6)
Increases (decreases) in cash or cash equivalents	806.9	(573.2)	1,423.4	(819.5)	351.7
Ratio of earnings to fixed charges under Mexican GAAP(2)	5.7x	1.2x	1.9x	1.5x	1.8x
Ratio of earnings to fixed charges under US GAAP(2)	10.4x	1.2x	1.9x	1.6x	1.9x
Total access lines in service (in thousands) (end of period)					
Business	132.4	177.6	228.0	295.6	311.8
Residential	216.7	275.9	377.9	497.0	620.5
Total	349.1	453.5	605.9	792.5	932.3

As of

December 31,

	2003	2004	2005	2006	2007
	(Constant Ps. in millions as of December 31, 2007)				
Balance Sheet Data:					
Cash and cash equivalents	1,191.5	618.3	2,041.7	1,222.1	1,573.9
Capital stock	7,926.0	7,926.0	8,677.8	8,677.8	8,870.1
Total assets	9,562.5	9,633.7	11,696.2	19,894.0	19,830.7
Total debt	2,551.8	2,447.5	3,061.3	8,473.9	7,757.0
Total liabilities	3,231.6	3,389.2	4,055.1	12,009.7	11,080.3
Total shareholders' equity	6,330.9	6,244.5	7,641.1	7,884.3	8,750.3
Net Assets	6,170.6	6,753.0	7,634.5	13,603.8	13,449.4
Dividends	—	—	—	—	—

Data in Accordance with US GAAP(3):

	Year Ended December 31,				
	2003	2004	2005	2006	2007
	(Constant Ps. in millions as of December 31, 2007)				
Financial Data:					
Income from operations	201.1	285.0	646.0	682.9	1,207.1
Income from continuing operations	3,222.7	81.7	537.5	212.6	1,120.5
Net income	3,222.7	81.7	537.5	212.6	1,120.5
Net income from operations per share	0.4	0.0	0.1	0.0	0.1
Capital stock	6,419.5	6,419.5	7,171.3	7,171.3	7,363.6
Shares outstanding	7,601,120,598	7,601,120,598	8,522,810,598	8,522,810,598	8,769,353,223
Total assets	9,059.8	9,296.9	11,760.5	20,407.3	20,495.2
Total debt	2,551.8	2,447.5	3,061.3	8,473.9	7,757.0
Total shareholders' equity	5,709.9	5,791.3	7,418.3	7,752.6	9,256.7

- (1) Other income for the year ended December 31, 2003 includes a net gain of Ps. 2,186.1 (US\$187.9 million) due to our repurchase of certain debt.
- (2) For purposes of determining the ratio of earnings to fixed charges, earnings are defined as our income from operations before income taxes, plus fixed charges. Fixed charges consist of interest expense on all

indebtedness, amortization of debt issuance costs and 33% of lease payments, which represents the amounts considered to be the interest factor.

(3) Reconciled in accordance with Note 24 of our consolidated financial statements.

Exchange Rates

As of April 25, 2008, the noon buying rate in the spot market for the purchase of US dollars (in nominal pesos per US dollar) was Ps. 10.47(1). The following table sets forth, for the periods indicated, the period end, average, high and low noon buying rates, in each case for the purchase of US dollars, all expressed in nominal pesos per US dollar.

Prior Years	Noon buying rate(1)			
	Period End	Average	High	Low
Year ended December 31, 2003.....	11.24	10.79	11.41	10.11
Year ended December 31, 2004.....	11.15	11.20	11.33	11.11
Year ended December 31, 2005.....	10.63	10.89	11.41	10.41
Year Ended December 31, 2006.....	10.80	10.91	11.46	10.43
Year Ended December 31, 2007.....	10.92	10.93	11.27	10.67

(1) Source: Federal Reserve Bank of New York

The following table sets forth, for the periods indicated, the high and low noon buying rates, in each case for the purchase of US dollars, all expressed in nominal pesos per US dollar.

Month/Year	Noon buying rate(1)	
	High	Low
October 2007	11.00	10.67
November 2007	10.91	10.70
December 2007.....	11.15	10.93
January 2008.....	10.97	10.82
February 2008.....	10.82	10.67
March 2008.....	10.85	10.63

(1) Source: Federal Reserve Bank of New York

B. Capitalization and Indebtedness

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

Risks Relating to Our Company

Our integration of Avantel is not completed yet and the combined business may fail to meet our expectations.

Our integration of the Axtel and Avantel businesses started in December 2006 and is not expected to be completed before year-end 2008. The integration process has required significant resources and management

attention and although no major delays or unforeseeable events have occurred thus far, we might face delays or currently unforeseen difficulties or impediments in the remaining integration process. Such delays or impediments could require significant expenditures to overcome and could postpone our ability to recognize cost savings from the integration, each of which would harm our profitability and cash flow. In addition, these challenges could divert management's attention from the operation and growth of our business, which could harm our revenues and profitability and cause us to grow more slowly than we currently anticipate. It is also possible that problems with the integration of the two businesses or a failure to anticipate certain issues arising in connection with the acquisition will prevent the combined business from meeting our current expectations. Our relative lack of experience in consummating acquisitions and integrating acquired businesses could increase these risks for us.

Our acquisition of Avantel in December 2006 could make it difficult for you to evaluate our historical performance and future prospects.

Because Axtel's acquisition of Avantel was consummated in December 2006, the historical financial information included in this Form 20-F covers only the 2007 period during which the two businesses were operated under common ownership. Accordingly, the historical financial information included in this Form 20-F may not reflect what our results of operations and financial condition would have been a combined entity during the years before 2007. Our limited operating history as a combined entity and the challenge inherent in concluding the integration of the previously independent businesses make evaluating our business and future financial prospects difficult. You should consider our potential for future business success and operating profitability in light of the risks, uncertainties, expenses and difficulties typically encountered by recently combined companies.

Our network growth strategy may fail to generate the revenues we anticipate.

From our inception through December 31, 2007, we have invested approximately Ps. 21,968.6 million in network and infrastructure. We anticipate making significant additional expenditures to maintain and upgrade our network, expand our network and business and to complete the integration of Avantel's network and business. These expenditures, together with operating expenses, may adversely impact our cash flow and profitability, particularly if the expenditures do not lead to additional revenue. We also anticipate that continued growth will require us to attract and retain qualified personnel necessary to efficiently manage such growth. If we are unable to meet the challenges that our growth presents, our results of operations and financial condition could be adversely affected.

Our increased leverage resulting from the acquisition of Avantel could significantly affect our growth and operating results.

We financed the acquisition of Avantel with approximately US\$516.0 million in debt. Although we reduced our level of debt during 2007, our total debt stood at US\$713.9 million as of December 31, 2007, a significantly larger amount compared to the pre-Avantel acquisition levels. The resulting increase in debt service costs could reduce the amount of cash which would otherwise be available to invest in expansion of our business or to meet other obligations. Likewise, our higher level of leverage could reduce our access to new financing sources on favorable terms, and accordingly, significantly limit our growth and adversely affect our operating results.

We have a history of substantial losses and expect to incur future losses.

We have incurred a cumulative net loss of Ps. 949.6 million from inception to December 31, 2007. We anticipate that we could continue to incur net losses in the future.

We depend on certain vendors for the deployment of our network.

Our ability to achieve our strategic objectives and our overall performance and prospects depends on and will depend on, in large part, the successful, timely and cost-effective acquisition and performance of telecommunications equipment including wireless access products, as well as WiMAX-based technology equipment currently being deployed. If any of our vendors, including Motorola de Mexico S.A. and Motorola Inc., which provides the "802.16e WiMAX technology" for a significant portion of our 2008 network access infrastructure

investments, are unable or fail to continue supplying products, or if WiMAX is not able to comply with the expected capabilities, our network expansion and growth could be slowed and our operating results could be adversely affected.

We depend on key personnel; if they were to leave us, we might have an insufficient number of qualified employees.

We believe that our ability to implement our business strategy and our future success depends on the continuous employment of our senior management team, in particular our president and chief executive officer, Tomás Milmo Santos. Our senior management team has extensive experience in the industry and is vital in maintaining some of our major customer relationships, which might be difficult to replace. The loss of the technical knowledge, management and industry expertise of these key employees could make it difficult for us to execute our business plan effectively and could result in delays in new products being developed, loss of customers and diversion of resources while we seek replacements.

If we do not successfully maintain, upgrade and efficiently operate accounting, billing, customer service and management information systems and successfully integrate Avantel's administrative operations, we may not be able to maintain and improve our operating efficiencies.

Sophisticated information and processing systems are vital to our operations and growth and our ability to monitor costs, render monthly invoices for services, process customer orders, provide customer service and achieve operating efficiencies. We have installed the accounting, information and processing systems that we deem necessary to provide services efficiently. However, there can be no assurance that we will be able to successfully operate and upgrade such systems or complete the migration of Avantel's operations onto such systems or that these systems will continue to perform as expected. Any failure in our information and processing systems could impair our ability to collect payment from customers and respond satisfactorily to customer needs.

Our operations are dependent upon our ability to protect our network infrastructure.

Our operations are dependent upon our ability to protect our network infrastructure against damage from fire, earthquakes, hurricanes, floods, power loss, breaches of security, software defects and similar events and to construct networks that are not vulnerable to the effects of such events. The occurrence of a natural disaster or other unanticipated problems at our facilities or at the sites of our switches could cause interruptions in the services we provide. The failure of a switch would result in the interruption of service to the customers served by that switch until necessary repairs were effected or replacement equipment was installed. Repairing or replacing damaged equipment may be costly. Any damage or failure that causes interruptions in our operations could have a material adverse effect on our business, financial condition and results of operations.

We depend on certain important customers for a significant portion of our revenues.

Our three largest customers generated approximately 19% of total revenues in 2007. Accordingly, our ability to maintain a satisfactory relationship with these customers has a direct impact on our revenues and profitability. If these customers breach some or all the conditions established in their respective commercial agreements, or such agreements are not renewed upon their respective expiration dates, our business, financial condition, revenues and results of operations could be adversely affected.

We depend on Telmex for interconnection and we may be forced to pay higher interconnection fees in the future, which could have a material adverse effect on our business and results of operations.

Telmex exerts significant influence on all aspects of the telecommunications markets in Mexico, including interconnection agreements. We use Telmex's network to terminate the vast majority of our customers' calls. The interconnection agreement between Axtel and Telmex was renewed in March 2008. However, it remained expired during renegotiations for 2006 and 2007 and we can provide no assurance that it will be extended before its expiration date on December 31, 2008. If Telmex breaches some or all the conditions established in the

interconnection agreement, or if we are not able to renew this agreement under acceptable terms upon its expiration, we might be forced to offer services that will no longer be profitable and competitive. In addition, if the *Secretaría de Comunicaciones y Transporte* (“SCT”) or the Mexican telecommunications regulatory authority (*Comisión Federal de Telecomunicaciones*, or “COFETEL”) ceased to regulate Telmex’s pricing, the resulting competitive climate could have a material adverse effect on our business, financial condition and results of operations.

We rely on Telmex to maintain our leased last-mile links.

We maintain a number of dedicated links and last-mile-access infrastructure under lease agreements with Telmex. If Telmex breaches the agreed contractual conditions, or an agreement is not renewed upon its expiration, and Telmex discontinues the provision of services before we are able to link these customers to our own network, there could be a material adverse effect on our operations and an adverse effect on our business, financial condition and results of operations.

We are currently dependent on intellectual property licensed from Verizon Communications (formerly MCI), which is necessary for our long-distance platform and for managing our long distance billing.

We are currently dependent on services provided by and on intellectual property licensed to us by Verizon Communications to manage the national and international long distance billing system that we acquired from Avantel. Our license agreement with Verizon Communications for this system expires in May 2008. We may not be able to migrate Avantel’s billing system onto our own platform before the license agreement expires. If we are not able to migrate that system, or to renew the agreement at all, we could experience operational and administrative disruptions which could adversely affect our business and results of operations.

One of our main access technology suppliers has filed for creditor protection under Canada’s CCAA (Companies’ Creditors Arrangement Act).

We buy from SRTelecom new equipment and spare parts for our Symmetry access technology solution. Currently, this vendor has filed for creditor protection under Canada’s CCAA, a similar status to U.S. Chapter 11. If the financial conditions of this vendor deteriorate, we could be adversely affected due to the lack of spare parts for the equipment already deployed jeopardizing the future of this technology. Damaged equipment would have to be replaced with another access solution in order to continue delivering services.

A system failure could cause delays or interruptions of service, which could cause us to lose customers.

To be successful, we will need to continue to provide our customers reliable service over our network. Some of the risks to our network and infrastructure include:

- physical damage to access lines;
- power surges or outages;
- software defects; and
- disruptions beyond our control.

Disruptions may cause interruptions in service or reduced capacity for customers, either of which could cause us to lose customers and incur additional expenses.

Under Mexican law, our concessions could be expropriated or temporarily seized.

Pursuant to the Mexican Federal Telecommunications Law (*Ley Federal de Telecomunicaciones*) enacted in 1995, the public telecommunications networks are considered public domain. Under such law, holders of concessions to install, operate and develop public telecommunications networks are subject to the provisions of the

Mexican Federal Telecommunications Law and any other provision contained in the concession title. The Mexican Federal Telecommunications Law provides, among other things, for the following:

- Rights and obligations granted under the concessions to install, operate and develop public telecommunications networks may only be assigned with the prior authorization of the SCT;
- Neither the concession nor the rights thereunder or the related assets may be assigned, pledged, mortgaged or sold to any government or country; and
- The Mexican government (through the SCT) may expropriate or temporarily seize the assets related to the concessions in the event of natural disasters, war, significant public disturbance or threats to internal peace or for other reasons relating to economic or public order.

Mexican law sets forth the process for indemnification for direct damages arising out of the expropriation or temporary seizure of the assets related to the concessions, except in the event of war. However, in the event of expropriation, we cannot assure you that the indemnification will equal the market value of the concessions and related assets or that we will receive such indemnification in a timely manner. Mexican law does not prohibit a grant of a security interest by the concessionaire to its creditors (except for security granted to a foreign government or country) in the concessions and the assets, provided that all procedural laws are complied with; however, if such security interest is enforced, the assignee must comply with the Mexican Federal Telecommunications Law's provisions related to concessionaires, including, among others, the requirement to receive the authorization by the SCT to be a holder of the concession.

The regulatory authorities could require us to offer services in certain geographical areas where we do not currently provide services, which could have a negative effect on our operating margins and results of operations.

The SCT has granted us the necessary permits to provide services in the whole Mexican territory. Some of our concessions require us to offer services in certain geographical areas where we do not currently provide services. With respect to those geographical areas in which we were required to provide such services by December 2007, we have complied with such coverage requirements. With respect to those geographical areas in which we are required to provide such services by December 2008, we expect to comply with any regulatory authorities requirements. However, if needed we may request the necessary extensions from the SCT in order to comply with the coverage requirements, which extensions we have been able to obtain from the SCT in the past. We may also be required to provide services in geographical areas where we may experience a low operating margin with respect to such services. If we do not obtain the necessary extensions when required, or if we are required to provide services in areas where we do not currently provide services or in geographical areas where we may experience a low operating margin with respect to such services, our results of operations and financial condition may be adversely affected.

We operate in a highly competitive environment, which may negatively affect our operating margins.

The telecommunications industry in Mexico is becoming more competitive. Over the past seven years, we have not increased prices for local and long distance services to our customers. Additionally, in 2006 the government enacted a new legislation and convergence policy, which established the guidelines for the provision of voice, data and video services by telecommunications companies, including bundled services. The new legal framework will facilitate the entrance of new participants into the Mexican telecommunications and data market, such as cable companies, broadcasting companies, and the state-monopoly Federal Electricity Commission (Comisión Federal de Electricidad, or "CFE"). Although it does not currently affect our operations directly, broadcasters such as Grupo Televisa, S.A. and TV Azteca S.A. de C.V. and cellphone service providers such as América Móvil S.A. de C.V. might be allowed to retain excess bandwidth in their networks, and if granted the corresponding concessions or amendments thereto, they will have the capability to provide services similar to those that we currently provide or intend to provide in the near future, including digital channels, internet service and IP telephony. We expect the Mexican telecommunications market to continue to experience rate pressure, primarily as a result of:

- increased competition and focus by our competitors on increasing market share;
- recent technological advances that permit substantial increases in the transmission capacity of both new and existing fiber-optic networks, resulting in long distance overcapacity and rate pressure;
- major participation of traditional fixed-line competitors;
- the entrance of cable television operators into certain of our markets; and
- the entrance of new competitors, such as broadcasting companies (Televisa or TV Azteca), or CFE.

As the telecommunications industry in Mexico becomes more competitive, we will face significant competition from other operators, primarily on the basis of features, pricing and customer service. Some of these competitors include Telmex, Alestra, S.A. de C.V. (“Alestra”) and Maxcom Telecomunicaciones, S.A.B. de C.V. (“Maxcom”), as well as established local cable television operators who may expand their services into certain of our markets, such as local and long distance voice and data service. As resellers of telephony services become licensed, they will also offer competition in many of our targeted markets.

Telmex, as the former state-owned telecommunications monopoly and dominant provider of local and other telecommunications services in Mexico, has significantly greater financial and other resources than those available to us. In addition, Telmex’s nationwide network and concessions, as well as its established and long-standing customer base, give it a substantial competitive advantage over us.

We might see a more aggressive competitive response from other telecommunication services providers.

With the acquisition of Avantel we have significantly increased our participation in Mexico’s telecommunications sector, especially in the business market. As a result, our larger presence might produce a more aggressive response from competitors, including Telmex. This response could include aggressive price cutting or targeting of significant customers, among others, and could have a material adverse effect on our business, financial condition and results of operations.

We depend on revenues from certain highly competitive markets.

High-volume business customers are among the most attractive niches in the telecommunications market. This niche is being pursued by a number of carriers that offer competitive telecommunications services solutions in order to gain these accounts. Losing some of these customers could lead to a significant loss of revenue and lower operating income.

We depend on revenues from long distance services.

Prices for long distance services have been declining as new products such as voice over internet protocol, or VoIP, continue to gain acceptance. If we are unable to replace revenues lost from long distance with revenues from other services, such as local, data or integrated services, we could have a material adverse effect on our business, financial condition and results of operations.

We may need additional financing.

We may require additional financing in the future to fund our operations. We cannot assure you that we will have sufficient resources and that, if needed, any financing will be available in the future or on terms acceptable to us. In addition, our ability to incur additional indebtedness will be restricted by the terms of agreements currently in place or into which we may enter in the future.

The technology we use may be made obsolete by the technology used by our competitors.

Our fixed wireless system, as well as our fiber optic network, point-to-multipoint and point-to-point infrastructure, may not be as efficient as technologies used in the future by our competition. We have relied heavily on the continued performance of wireless technology. Technological changes or advances in alternative technologies may adversely affect our competitive position and require us to reduce our prices, substantially increase capital expenditures and/or write down obsolete technology.

If our current churn rate increases, our business could be negatively impacted.

The cost of acquiring a new customer is much higher than the cost of maintaining an existing customer. Accordingly, customer deactivations, or churn, could have a material negative impact on our operating income, even if we are able to obtain one new customer for each lost customer. Our average monthly churn rate has been stable during the last 24 months at approximately 1.3%, which is higher than that of our main competitor. Our churn rate mainly results from customer deactivations due to non-payment of bills. If we experience an increase in our churn rate, our ability to achieve revenue growth could be materially impaired. In addition, a decline in general economic conditions could lead to an increase in churn, particularly among our residential customers.

We are obligated to comply with certain restrictions under our existing indebtedness, which may affect our future activities.

Under (i) the indenture governing our 11% senior notes due 2013, (ii) our term loan facility, and (iii) the indenture governing our 7 5/8% senior notes due 2017, we will be obligated to comply with certain covenants, which may restrict our ability to pay dividends, carry out acquisitions, incur indebtedness or engage in other transactions, including certain financings.

Risks Relating to the Mexican Telecommunications Industry

We operate in a highly regulated industry.

As a provider of public services, we are subject to extensive regulation. Although the basic regulatory framework governing telecommunications has been in existence since 1995, it may undergo changes from time to time, including changes that may materially and adversely affect our business, operations, financial condition and prospects.

If the Mexican government grants more concessions or amends existing concessions, the value of our concessions could be severely impaired.

The Mexican government regulates the telecommunications industry. Our concessions are not exclusive and the Mexican government has granted and may discretionary grant additional concessions covering the same geographic regions. We cannot assure you that additional concessions to provide services similar to those we provide will not be granted and that the value of our concessions and competition levels will not be adversely affected as a result.

Fraud could increase our expenses.

The fraudulent use of telecommunications networks could impose a significant cost upon service providers, who must bear the cost of services provided to fraudulent users. We may suffer a loss of revenue as a result of fraudulent use and incur an additional cash cost due to our obligation to reimburse carriers for the cost of services provided to fraudulent users. Although technology has been developed to combat this fraudulent use and we have installed it in our network, this technology does not eliminate fraud entirely. In addition, because we rely on other long distance carriers to terminate our calls on their networks, some of which do not have anti-fraud technology in their networks, we may be particularly exposed to this risk in our long distance service.

Risks Relating to Mexico

Macroeconomic developments in Mexico affect our business.

We are a Mexican company with all of our operations in Mexico. The economic environment within Mexico can have a significant impact on our business and financial condition and results of operations.

Beginning in December 1994 and continuing through 1995, Mexico experienced an economic crisis characterized by a sharp devaluation of the peso, high inflation, foreign currency exchange rate instability, high domestic interest rates, a strong contraction in consumer demand for many products and services, reduced availability of credit, high unemployment and diminished international investor confidence in Mexico. Mexico's gross domestic product, which grew at a real annual rate of 4.4% during 1994, declined by 6.2% in real terms during 1995.

In response to these developments, beginning in February 1995, the Mexican government implemented a variety of economic programs designed to promote economic recovery, stabilize foreign currency exchange rates and reduce inflation. Economic conditions in Mexico improved moderately in 1996 and 1997. However, a combination of factors led to a slowdown in Mexico's economic growth in 1998. Notably, the decline in the international price of oil resulted in a reduction of federal revenues, approximately one-third of which are derived from petroleum taxes and duties. In addition, the economic crises in Asia and Russia, as well as the financial turmoil in Brazil and elsewhere, produced greater volatility in the international financial markets, which further slowed Mexico's economic growth. In 1998, the inflation rate in Mexico was 18.6%, interest rates on 28-day Certificados de la Tesorería de la Federación ("CETES") averaged 24.6% and the peso lost 22.7% of its value (in nominal terms) relative to the US dollar.

During 1999, conditions improved with inflation in Mexico at 12.3%, interest rates on 28-day CETES averaging 21.3% and the peso appreciating 4.0% in value (in nominal terms) relative to the US dollar. Throughout 2000, the improvement shown in 1999 continued. In 2000 the inflation rate was 9.0%, interest rates on 28-day CETES averaged 15.3% and the peso devalued 1.2% in value (in nominal terms) relative to the US dollar. The Mexican government estimated that Mexico's real gross domestic product grew by 5.0% in 1998, 3.8% in 1999 and 6.6% in 2000.

Beginning in January 2001, however, and increasing in the fourth quarter of 2001, amid concerns of a global economic slowdown and a recession in the United States, Mexico began to experience an economic slowdown marked by a decline in gross domestic product. In 2001, Mexico's gross domestic product shrank by 0.2% in real terms while the inflation rate was 4.4%, interest rates on 28-day CETES averaged 11.3% and the peso appreciated 4.6% in value (in nominal terms) relative to the US dollar. During 2002, as the United States and global economic slowdown continued, the Mexican real gross domestic product growth rate was 0.6%, the inflation rate was 5.7%, interest rates on 28-day CETES averaged 7.1% and the peso devalued 13.8% (in nominal terms) relative to the US dollar. During the years ended December 31, 2003, 2004 and 2005, the inflation rate was 4.0%, 5.2% and 3.3%, respectively, interest rates on 28-day CETES averaged 6.2%, 6.8% and 9.2%, respectively, and the peso devalued 7.6% and appreciated 0.8% and 4.6%, respectively (in nominal terms), relative to the US dollar. In 2006 and 2007, the inflation rate was 4.1% and 3.8% respectively, interest rates on 28-day CETES averaged 7.0% and 7.2% respectively, and the peso appreciated 4.6% and depreciated 1.1% (in nominal terms) respectively, relative to the US dollar. The gross domestic product for 2003, 2004, 2005, 2006 and 2007 was 1.3%, 4.4%, 3.0%, 4.8% and 3.3%, respectively.

In the past, inflation has led to high interest rates and devaluation of the peso. Inflation itself, as well as governmental efforts to reduce inflation, has had significant negative effects on the Mexican economy in general and on Mexican companies, including us. Inflation in Mexico decreases the real purchasing power of the population of Mexico, and the Mexican government's efforts to control inflation by tightening the monetary supply have historically resulted in higher financing costs, as real interest rates have increased. Such policies have had and could have an adverse effect on us.

A global economic slowdown or other future economic developments in or affecting Mexico could impair our business, results of operations, financial condition, prospects and ability to obtain financing.

Political events in Mexico could affect Mexican economic policy and our results of operations.

The Mexican government has exercised, and continues to exercise, significant influence over the Mexican economy. Mexican governmental actions concerning the economy could have a significant impact on Mexican private sector entities in general, as well as on market conditions.

In the Mexican national elections held on July 2, 2006, Felipe Calderón of the Partido Acción Nacional, or “PAN,” won the presidency. He succeeded Vicente Fox, of the same party. During the July elections, members of the Mexican Congress were also elected. The PAN obtained the largest number of seats in both houses of the Mexican Congress, but not enough to secure an absolute majority. The second-largest political party in the Mexican Congress is now the left-wing Partido de la Revolución Democrática, or “PRD.” The Partido Revolucionario Institucional, or “PRI,” who had the presidency for over 70 years, became the third force in Congress after July elections. The presidential election campaigns were extremely competitive, with significant confrontations, mainly between the PAN and PRD. President Calderón was elected with a less-than-1% margin of victory over PRD’s candidate, Andres Manuel López Obrador. The hard-fought campaigns together with the close results generated street blockades, protests, and even the attempt by the PRD to obstruct President Calderón’s inauguration ceremony on December 1, 2006. During the first year of President Calderon there has been significant confrontation from the PRD group in the Congress leaving the federal government with the PRI as the only alternative to negotiate important reforms. We expect this intense political struggle to continue or even intensify in the Mexican Congress, which could lead to a further slowdown in the progress of political and economic reforms in Mexico. This gridlock could have an adverse effect on us, including our business, financial condition, prospects and results of operations.

Felipe Calderón’s presidency may also bring significant changes in laws, public policies and/or regulations that could adversely affect Mexico’s political and economic situations, which could adversely affect our business. Mexico will next hold elections to elect members of the Mexican congress in July 2009.

Social and political instability in Mexico or other adverse social or political developments in or affecting Mexico could adversely affect us and our ability to obtain financing. It is possible that political uncertainty may adversely affect financial markets.

High interest rates in Mexico could increase our financing and operating costs.

Mexico historically has had high real and nominal interest rates. The interest rates on 28-day Mexican government treasury securities, CETES, averaged 21.3%, 15.3% and 11.3% for 1999, 2000 and 2001, respectively. Although average rates for 2002, 2003, 2004, 2005, 2006 and 2007 were 7.1%, 6.2%, 6.8%, 9.2%, 7.0% and 7.2% respectively, we cannot assure you that interest rates will remain at their current rates. Thus, if we are forced to incur Mexican peso-denominated debt in the future, it may be at interest rates higher than the current rates.

We may lose money because of peso devaluation.

While our revenues are almost entirely denominated in pesos, the substantial majority of our obligations, and 77.8% of our debt as of December 31, 2007 is denominated in US dollars. The value of the Mexican peso has been subject to significant fluctuations with respect to the US dollar in the past and may be subject to significant fluctuations in the future. During the year ended December 2004 and 2005, the peso was appreciated 0.8% and 4.6%, respectively (in nominal terms) relative to the US dollar. In 2006 and 2007, the peso depreciated 1.6% and 1.1% (in nominal terms) respectively, relative to the US dollar. Further declines in the value of the peso relative to the US dollar could adversely affect our ability to meet our US dollar-denominated obligations.

Our financial statements do not give you the same information as financial statements prepared under United States accounting principles.

We prepare our financial statements in accordance with Mexican GAAP. These principles differ in significant respects from US GAAP, including, but not limited to, the treatment of the capitalization of pre-operating expenses, the amortization of frequency rights, the capitalization of interest and deferred income taxes and employees' profit sharing, and in the presentation of cash flow information. In particular, all Mexican companies must incorporate the effects of inflation directly in their accounting records and in published financial statements. For these and other reasons, the presentation of Mexican financial statements and reported earnings may differ from that of companies in other countries. See Note 25 of our consolidated financial statements.

Risks Relating to the Financial Obligations of the Company

Our indebtedness could adversely affect our financial condition and impair our ability to fulfill our obligations under the notes.

Our ability to meet our debt service requirements will depend on our future performance, which is subject to a number of factors, many of which are outside our control. We cannot assure you that we will generate sufficient cash flow from operating activities to meet our debt service and working capital requirements.

As of December 31, 2007, we had approximately Ps. 7,757.0 million of debt and accrued interest and our ratio of net debt to Adjusted EBITDA for the twelve months ended December 31, 2007 was 1.5x.

Our level of indebtedness may have important negative effects on our future operations, including:

- impairing our ability to obtain additional financing in the future for working capital, capital expenditures, acquisitions or other general corporate purposes;
- requiring us to dedicate a substantial portion of our cash flow to the payment of principal and interest on our indebtedness, which reduces the availability of our cash flow to fund working capital, capital expenditures, acquisitions and other general corporate purposes;
- subjecting us to the risk of increased sensitivity to interest rate increases on our indebtedness with variable interest rates, including our borrowings under our credit facilities;
- increasing the possibility of an event of default under the financial and operating covenants contained in the agreements governing our and our subsidiary guarantors' outstanding indebtedness; and
- limiting our ability to adjust to rapidly changing market conditions, reducing our ability to withstand competitive pressures and making us more vulnerable to a downturn in general economic conditions or our business than our competitors with less debt.

If we are unable to generate sufficient cash flow from operations in the future to service our debt, we may be required to refinance all or a portion of our existing debt, or to obtain additional financing. We cannot assure you that any such refinancing would be possible or that any additional financing could be obtained. Our inability to obtain such refinancing or financing may have a material adverse effect on us.

We and our subsidiary guarantors may incur substantially more debt, which could further exacerbate the risks associated with our indebtedness.

We may be able to incur substantial additional debt in the future. Although the agreements governing our and our subsidiary guarantors' outstanding indebtedness contain restrictions on the incurrence of additional indebtedness, these restrictions are subject to a number of qualifications and exceptions, and the indebtedness incurred in compliance with these restrictions could be substantial. Also, these restrictions do not prevent us or our subsidiary guarantors from incurring obligations that do not constitute "indebtedness" as defined in the relevant

documents. Adding new debt to our current indebtedness levels would increase our leverage. The related risks that we now face could intensify.

The instruments governing our indebtedness contain cross-default provisions that may cause all of the debt issued under such instruments to become immediately due and payable as a result of a default under an unrelated debt instrument.

Instruments governing our indebtedness contain certain affirmative and negative covenants and require us and our subsidiaries to meet certain financial ratios and tests. Our failure to comply with the obligations contained in these instruments governing our indebtedness could result in an event of default under the applicable instrument, which could then result in the related debt and the debt issued under other instruments becoming immediately due and payable. In such event, we would need to raise funds from alternative sources, which may not be available to us on favorable terms, on a timely basis or at all. Alternatively, such default could require us to sell our assets and otherwise curtail operations in order to pay our creditors.

Restrictive covenants in our debt agreements may restrict the manner in which we can operate our business.

The agreements governing our and our subsidiary guarantors' outstanding indebtedness limit, among other things, our ability and the ability of our restricted subsidiaries to:

- borrow money or issue guarantees;
- pay dividends, redeem capital stock or make other restricted payments;
- create liens to secure indebtedness;
- make certain investments;
- sell certain assets;
- pledge assets;
- participate in joint-venture agreements;
- enter into transactions with our affiliates; and
- merge with another entity or sell substantially all of our assets.

If we fail to comply with these covenants, we would be in default under our credit facility and the indentures, and the principal and accrued interest on our outstanding indebtedness may become due and payable. In addition, our future indebtedness agreements may contain additional affirmative and negative covenants which could be more restrictive than those contained in the instruments governing our existing indebtedness.

We may not be able to make payments in US dollars.

In the past, the Mexican economy has experienced balance of payments deficits and shortages in foreign exchange reserves. While the Mexican government does not currently restrict the ability of Mexican or foreign persons or entities to convert pesos to foreign currencies, including US dollars, it has done so in the past and could do so again in the future. We cannot assure you that the Mexican government will not implement a restrictive exchange control policy in the future. Any such restrictive exchange control policy could prevent or restrict our access to US dollars to meet our US dollar obligations and could also have a material adverse effect on our business,

financial condition and results of operations. We cannot predict the impact of any such measures on the Mexican economy.

Payment of judgments entered against us in Mexico will be in pesos, which may expose you to exchange rate risks.

If proceedings to enforce our obligations under the notes are brought in Mexico, Mexican law permits us to pay a resulting judgment in pesos. Under the *Ley Monetaria de México* (the “Mexican Monetary Law”), an obligation payable in Mexico in a currency other than pesos may be satisfied in pesos at the exchange rate in effect on the date the payment is made. This rate is currently determined and published by the Banco de Mexico every business day.

Under Mexico’s *Ley de Concursos Mercantiles* (the “Mexican Bankruptcy Law”), upon our declaration of insolvency or bankruptcy, or in the event that actions and claims are initiated in the courts of Mexico, our obligations under the notes:

- (i) would be converted into pesos at the exchange rate published by the Banco de Mexico prevailing at the time of such declaration and would subsequently be converted into Unidades de Inversion, which is a unit pegged to the consumer price index determined by Banco de Mexico, and payment would occur at the time claims of our other creditors are satisfied;
- (ii) would be subject to any provisional remedy (“*providencia precautoria*”) which may be issued in such proceedings;
- (iii) would be dependent upon the outcome of the insolvency or bankruptcy proceedings;
- (iv) would not be adjusted to take into account depreciation of the peso against the dollar occurring after such declaration of insolvency or bankruptcy; and
- (v) would be subject to certain statutory preferences including tax, social security and labor claims and secured creditors.

Under the Mexican Bankruptcy Law, it is possible that in the event we are declared bankrupt, any amount by which the stated principal amount of the notes exceeds their accreted value may be regarded as not mature and, therefore, claims of holders of the notes may only be allowed to the extent of the accreted value of the notes. It is believed that there are no Mexican precedents in bankruptcy addressing this point and there exists significant uncertainty as to how a Mexican court would measure the claims to holders of the notes, particularly given the recent enactment of the Mexican Bankruptcy Law in May 2000.

Item 4. INFORMATION ON THE COMPANY

A. History and Development of the Company

Axtel, S.A.B. de C.V. was founded in 1994. We are a variable capital corporation (*sociedades anonimas de capital variable*) organized under the laws of Mexico. In June 1996, we were awarded by the Mexican government a concession to install and operate a public telecommunications network for the offering of local and long distance telephony services in Mexico. In 1998 and 1999, we won several spectrum auctions, including for 60 MHz at 10.5 GHz for point-to-multipoint access, for 112 MHz at 15 GHz for point-to-point backhaul access, for 100 MHz at 23 GHz for point-to-point last mile access and for 50 MHz at 3.4 GHz for fixed wireless access, which together allow us to service the entire territory of Mexico. In June 1999, we launched commercial operations in the city of Monterrey.

We are the largest fixed-line integrated telecommunications company in Mexico after Telmex, providing local and long distance telephony, broadband Internet, data services, web hosting, information security services,

virtual private networks, and a wide range of integrated telecommunications services in twenty seven of the largest metropolitan areas in Mexico (Mexico City, Monterrey, Guadalajara, Puebla, Toluca, Leon, Queretaro, San Luis Potosi, Aguascalientes, Saltillo, Ciudad Juarez, Tijuana, Torreón (Laguna Region), Veracruz, Chihuahua, Celaya, Irapuato, Ciudad Victoria, Reynosa, Tampico, Cuernavaca, Mérida, Morelia, Pachuca, Hermosillo, San Juan del Rio and Xalapa.) at the end of 2007, which represent more than 44% of the total population of Mexico, according to the National Institute of Geography, Statistics and Information Technology of Mexico ("INEGI"). We estimate that our total lines represent approximately 10.3% of the lines in service of our total addressable market in the 27 cities we serviced at the end of 2007.

On October 25, 2006, we agreed with Banamex, and Telecomunicaciones Holding Mx, S. de R.L. de C.V. ("Tel Holding"), former controlling shareholders of Avantel, to purchase substantially all of the assets of Avantel Infraestructura, S. de R.L. de C.V. ("Avantel Infraestructura") for US\$485.0 million. We also agreed to purchase the equity interests of Avantel Infraestructura and Avantel, S. de R.L. de C.V. ("Avantel Concesionaria," both companies together being referred to as "Avantel") and each of Avantel's subsidiaries for US\$31.0 million. Following receipt of all required approvals from Axtel's shareholders and government regulators, we completed the acquisition on December 4, 2006. To finance the acquisition of Avantel, we used the proceeds from a dollar-denominated Ps. 3,383.4 million (US\$311.0 million) bridge loan facility, a peso and dollar Ps. 2,241.7 million term loan facility and cash on hand. We also paid value added tax, property transfer tax and other taxes related to the purchase of substantially all the assets of Avantel Infraestructura. On March 06, 2007, Mexico's *Servicio de Administración Tributaria* refunded Axtel Ps. 773.9 million corresponding to value added tax on the assets purchased from Avantel Infraestructura.

In relation to our acquisition of Avantel, we also entered into a Series B Shares subscription agreement with Tel Holding, an indirect subsidiary of Citigroup, Inc., for an amount equivalent to up to 10% of Axtel's common stock. On December 22, 2006 pursuant to the Subscription Agreement, we received a notice from Tel Holding confirming that it acquired 533,976,744 Series B Shares (represented by 76,282,392 CPOs) from the Mexican Stock Exchange (Bolsa Mexicana de Valores, or "BMV") and confirming its intention to subscribe and pay for 246,453,963 new Series B Shares (represented by 35,207,709 CPOs). On January 4, 2007, Tel Holding subscribed and paid for 246,453,963 new Series B Shares through the CPOs Trust. From January 4, 2007 through January 20, 2007, during the subscription period, other shareholders subscribed and paid 88,662 new Series B Shares through the CPOs Trust as well. New Series B Shares were subscribed and paid at Ps. 1.52 pesos each, generating Ps. 374.7 million in proceeds for Axtel.

Avantel is a Mexican corporation which provides telecommunications services to business, government and residential customers in Mexico. Avantel was incorporated as a 55.5%-44.5% joint-venture between Banamex and MCI in 1994 primarily oriented to provide national and international long-distance services. The sharp decline in national and international long-distance tariffs in Mexico (over 60% from 1997 to 2005) led Avantel to redesign its business strategy to focus on providing data and bundled value-added voice services to business customers. Avantel brought to Axtel valuable spectrum in various frequencies, approximately 390 kilometers of metropolitan fiber optic rings, 7,700 kilometers of long-distance fiber optic network, a robust IP backbone and connectivity in 200 cities in Mexico, among others.

The integration of Avantel enhanced our portfolio of products and services and also allows us to expand in existing cities and into new geographies more efficiently due to the complementary condition of Axtel's hybrid wireline and fixed-wireless local access network with Avantel's long-haul fiber optic network and strong data capabilities. We expect that most of our growth will come from continued customer acquisitions and build out of our network within our current markets as we continue to expand our coverage and capacity in the major metropolitan areas that we currently serve. We also expect to expand into selected markets we do not yet serve through organic growth and, possibly, strategic acquisitions or commercial agreements. For a description of our principal capital expenditures, see Item 5 "Liquidity and Capital Resources."

Our corporate offices are located at Blvd. Gustavo Diaz Ordaz km. 3.33 No. L-1, Col. Unidad San Pedro, San Pedro Garza Garcia, N.L., Mexico, CP 66215 (Telephone +52 (81) 8114-0000).

Our agent for service in the United States is CT Corporation System, located at CT 111 Eighth Avenue, 13th Floor, New York, New York 10011.

B. Business Overview

a) Our Company

We are the second-largest, and one of the fastest growing, fixed-line, integrated telecommunications company in Mexico, measured in revenues and EBITDA. We offer a wide array of services, including local and long distance telephony, broadband Internet, data and built-to-suit communications solutions in 27 cities and long distance telephone in 200 cities to more than 850,000 business and residential customers. In 2007, we generated revenues and operating income of Ps. 12,190.6 million (US\$1,121.9 million) and Ps. 1,393.8 million (US\$128.3million), respectively.

We provide services using a hybrid wireline and fixed wireless local access network (including 1,366.0 kilometers of metro fiber optic rings) along with 7,700 kilometers of long-haul fiber-optic network. Our last-mile access, designed to optimize capital expenditures through the deployment of network access equipment based on specific customer requirements, includes 37 digital switches, 431 fixed wireless access sites, 190 point-to-multipoint sites (of which 169 are within fixed wireless access sites) and 1,555 point-to-point wireless sites. Our nationwide long-haul network includes 7,700 kilometers of fiber optic network with links to terminate long-distance traffic in over 200 cities. As of December 31, 2007 we have invested in the aggregate approximately Ps. 21,968.6 million in network and infrastructure.

Our strategy is to continue to penetrate our existing markets by offering a comprehensive portfolio of high quality, facilities-based voice, data, internet, integrated solutions and value-added communications services and to cost-effectively enter into selective new markets with high growth and revenue opportunity. Our approach is to bundle multiple voice, data and Internet services into integrated telecommunications solutions for businesses and high-usage residential customers. We also intend to continue servicing foreign carriers with international traffic termination, as well as providing custom-made integrated telecommunications services to large corporate customers. For the twelve months ended December 31, 2007, approximately 78% of our revenues were generated from business customers and 22% of our revenues were generated from residential customers.

Axtel was founded in 1994 and in June 1996 was awarded by the Mexican government a concession to install and operate a public telecommunications network for the offering of local and long distance telephony services in Mexico. On December 4, 2006, Axtel acquired Avantel, adding an IP-based nationwide telecommunications network. After the acquisition, we hold the following spectrum assets: two concessions at 929 MHz for radio-messaging services, 56 MHz at 7 GHz for nationwide long-haul point to point transport, 120 MHz at 10.5 GHz in three regions and 60 MHz in the other six regions for point to multi-point access; 168 MHz at 15 GHz, 368 MHz at 23 GHz for nationwide point to point transport and 112 MHz at 37 to 38.6 GHz in five regions.

We provide local, long distance, data, internet, integrated solutions and value-added communications services in 27 of the largest metropolitan areas in the country, including Mexico City, Monterrey, Guadalajara, Puebla, Toluca, León, Querétaro, San Luis Potosí, Saltillo, Aguascalientes, Ciudad Juárez, Tijuana, Torreón (Laguna Region), Veracruz, Chihuahua, Celaya, Irapuato, Cd. Victoria, Reynosa, Tampico, Cuernavaca, Merida, Morelia, Pachuca, Hermosillo, San Juan del Rio and Xalapa. These 27 cities represent more than 44 of the total population of Mexico according to INEGI. We estimate that our total lines represent approximately 10.3% of the lines in service of our total addressable market in the 27 cities in which we provide local services. Additionally, our long-haul network provides long-distance services in over 200 cities across the country. We expect our growth will come from both continued customer acquisitions and the build out of our network within our current markets and in selected new cities as we continue to expand our coverage and capacity in the major metropolitan areas of Mexico.

In December 2007, we entered into an agreement with Motorola de Mexico S.A. de C.V. and Motorola Inc. to integrate WiMAX technology into AXTEL's Network. Additionally, we signed an agreement with the Mexican

Federal Electricity Commission (CFE) to have access to their extensive fiber optic network and increase our capacity of provisioning private line and data services in the country.

In the last couple of weeks of 2007, we were able to extend our business agreement with Nextel de México to continue providing Nextel de Mexico with local services, spectrum, long distance calling and 01-800 numbers, and other services, in a significant number of Mexican cities until August 31, 2011.

b) Competitive Strengths

Leading Market Position. By being one of the first competitive providers to approach customers with bundled local, long distance voice and data services in a significant number of cities across the country, we believe that we are able to meet pent-up demand for an alternative service provider, as well as establishing brand awareness and customer relationships prior to market entry by emerging competitors. We have benefited from our “first-competitor-to-market” advantage by capturing what we estimate to be approximately a 10.3% share of our total addressable market in the 27 cities where we offer local services. In Monterrey and Guadalajara, the first two markets where Axtel launched operations in 1999, we estimate that we have achieved an approximately 16% and 14%, respectively, share of our coverage market in each of these cities.

Comprehensive Voice and Data Service Portfolio. We provide our customers an integrated bundle of services that includes local and long distance voice services, as well as internet, data and other value-added services. We believe our comprehensive service portfolio enables us to build strong, long-term relationships with customers and increase our return on our investment in network infrastructure. Furthermore, our digital access, transport and innovative last-mile technologies enable us to meet the growing demand for data services.

Scalable Digital Network. Our hybrid fixed wireless and wireline local access network structure allows us to enter new markets quickly and cost-effectively. By utilizing the fixed wireless access technology model, we are able to quickly cover a substantial geographic area with reduced initial capital expenditures. We defer most incremental capital expenditures for last-mile connectivity until the customer subscribes to our service. As of December 31, 2007, our network consisted of 37 digital switches, 431 fixed wireless access sites, 190 point-to-multipoint sites (of which 169 are within fixed wireless access sites), 1,555 point-to-point radio links and 1,366 kilometers of metropolitan fiber optic rings. As of December 31, 2007, we have invested in the aggregate approximately Ps. 21,968.6 million in network and infrastructure to build an extensive local and national telecommunications network.

Flexible and Innovative Technology – Our capability to add new last-mile technologies allow us to continuously satisfy the changing requirements of existing and new customers. The deployment of 802.16e WiMAX, a new IP-based voice and data wireless technology designed to deliver voice and data solutions, under fixed, portable, nomadic and mobile environments, increases our capabilities to provide high-quality voice and data access solutions.

Scale—Second-Largest Fixed-Line Integrated Telecommunications Company in Mexico. We are the largest local, national and international long-distance and data services provider in Mexico, measured in lines in service, revenues and EBITDA, after the incumbent.

Compelling Financial Profile. We have favorable EBITDA generation (Ps. 4,084.5 million in 2007) and solid financial ratios with net debt to Adjusted EBITDA and Adjusted EBITDA to net interest expense of 1.5x and 5.2x, respectively, for the twelve months ended December 31, 2007.

Experienced Management Team and Internationally Renowned Equity Partners. Our senior management team has extensive entrepreneurial, financial, marketing and telecommunications expertise. The diverse experience

of our senior management team has contributed significantly to our initial success and rapid growth. In addition, we have benefited from working with strong local partners and experienced multinational investors such as The Blackstone Group, Citigroup Inc. and AIG-GE's Latin American Infrastructure Fund. Our local investors and directors include, among others, Tomás Milmo Santos, Thomas Milmo Zambrano, Alberto Santos de Hoyos, Lorenzo Zambrano Treviño and Banamex. These investors have extensive financial, operating and senior management experience in large Mexican corporations.

c) Strategy

The key elements of our business strategy are:

Target Service Sectors with High Profitability Potential. We have divided our target market into the residential market and business market. In the residential market, we focus on high-usage residential customers. Within the business market, we address the needs of micro and small business as well as medium and large companies, multinationals, financial institutions and government entities. We have developed differentiated, targeted telecommunications services plans designed to capture business and retain high-usage customers in each market. We believe that by focusing on the business and high-usage residential customers within a coverage area we are able to increase the return per dollar invested in our network infrastructure. For the twelve-month period ended December 31, 2007, approximately 78% of our revenues were generated from business customers and 22% from residential customers.

Bundle Products in an Integrated Offering. We believe that the bundling of voice, data and internet services into communications solutions for our customers enables us to generate higher revenue per customer and more revenue per dollar invested in access infrastructure while also generating customer loyalty. We have focused and will continue to focus on increasing the penetration of bundled products to our customer base. By being a facilities-based telecommunications service provider, we believe we are well positioned to offer our customers the convenience of receiving voice, data and internet services from a single provider.

Service Fast Growing Business Data Market. For corporate customers, financial institutions and government entities, we offer integrated solutions based on the specific needs of the customers, including design, implementation, maintenance and monitoring of their networks. For medium-size clients, we bundle voice and data packages that specifically meet their requirements in a cost-efficient way.

Maintain Voice Revenues Stream. Although data market represents an attractive and expanding revenues opportunity compared to slow growing voice-related revenues, still over 70% of Mexican telecommunications industry revenues is voice related. Significant voice revenues stream provides the leverage to further penetrate fast-growing data market.

Exploit "First-Competitor-to-Market" Advantage. As Telmex's primary and largest competitor in local fixed telephony services and one of the first facilities-based telecommunications service providers to enter new markets and offer integrated voice, data and internet services, we will continue to focus on selectively opening new markets where we believe we can capitalize on anticipated growth in that market and the market's desire to have an alternative carrier.

Focus on Customer Service and Retention. Since launching operations, we have been focused on achieving customer satisfaction levels that are superior to the incumbent and our primary competitors. We believe that our service-driven customer care leads to superior customer satisfaction, which enhances profitability and cash flow by increasing customer retention and expanding sales opportunities.

Continue to Expand Technologically Advanced Network Infrastructure. We continuously evaluate opportunities for network expansion both within our existing cities and additional regions in order to enhance our coverage area. We believe that selectively expanding our network and coverage area will enhance our ability to acquire large business customers with multi-city operations, which we expect to result in higher revenues and margin improvements while minimizing capital expenditures. We may also expand our network or operations

through acquisitions or commercial agreements, as we believe there may be additional opportunities for consolidation in the Mexican telecommunications industry. We are not currently engaged in formal negotiations with any company regarding a potential acquisition or commercial agreement but may engage in conversation with third parties from time to time regarding strategic acquisitions or combinations.

d) Products and Services

We offer a wide variety of telecommunications services, including, local, long distance, Internet, and data services, such as virtual private lines, dedicated private lines, frame relay and web-hosting. We also provide integrated telecommunications services such as network monitoring, call center outsourcing and LAN design, operation and maintenance services.

The following chart summarizes each component of our revenue sources for the full fiscal years ended December 31, 2006 and 2007:

	2007	2006	
Revenue Source	% Revenues	% Revenues	Description
Local services.....	43%	65%	We generate revenue by enabling our customers to originate and receive an unlimited number of calls within a defined local service area. Customers are charged a flat monthly fee for basic service, a per call fee for local calls (“measured service”), a per minute usage fee for calls completed on a cellular line (“calling party pays,” or CPP calls) and a monthly fee for value added services.
Long distance services ..	13%	9%	We generate revenues by providing long distance services for our customers’ completed calls.
Data and private lines....	21%	7%	We generate revenues by providing Internet, data and network services, like virtual private networks and dedicated private lines.
International traffic.....	10%	8%	We generate revenues terminating international traffic from foreign carriers.
Other services.....	13%	11%	We generate revenues from other services, which include among others, activation fees, and customer premises equipment (“CPE”) for new customers as well as custom-made integrated telecommunications services to corporate customers.
Total	100%	100%	

We offer the following products and services:

<u>Voice</u>	<u>Data</u>
Business and Residential Line	<ul style="list-style-type: none">• Local and Domestic Private Lines
<ul style="list-style-type: none">• Long Distance	<ul style="list-style-type: none">• High Speed Private Lines
<ul style="list-style-type: none">• Digital Trunks	<ul style="list-style-type: none">• Co-location
<ul style="list-style-type: none">• Voicemail	<ul style="list-style-type: none">• Virtual Private Networks (MPLS)
<ul style="list-style-type: none">• Centrex Line	<u>Internet</u>
<ul style="list-style-type: none">• Customer Premise Equipment	<ul style="list-style-type: none">• Dial Up Internet
<ul style="list-style-type: none">• Telephone Sets, Key Systems and PBX	<ul style="list-style-type: none">• Dedicated Internet
<ul style="list-style-type: none">• Call Waiting, Call Forwarding, Caller ID, Conference Call	<ul style="list-style-type: none">• Web Hosting
<ul style="list-style-type: none">• Directory Assistance	<ul style="list-style-type: none">• Internet on Demand
<ul style="list-style-type: none">• Operator Services	<ul style="list-style-type: none">• Internet FWA
<ul style="list-style-type: none">• Automatic Dialing	<ul style="list-style-type: none">• Co-location
<ul style="list-style-type: none">• Unique number	<u>Integrated Services:</u>
<ul style="list-style-type: none">• Prepaid Services	<ul style="list-style-type: none">• Data Centers
<ul style="list-style-type: none">• Collect Calls	<ul style="list-style-type: none">• Network Monitoring
<ul style="list-style-type: none">• Virtual Line	<ul style="list-style-type: none">• Contact Centers
<ul style="list-style-type: none">• Toll Free Services	<ul style="list-style-type: none">• Network Security Monitoring
<u>Bundles:</u>	<ul style="list-style-type: none">• LAN Maintenance
<ul style="list-style-type: none">• Axtel in a Box	<ul style="list-style-type: none">• LAN Design and Operation
<ul style="list-style-type: none">• Axtle NeXt	
<ul style="list-style-type: none">• Axtelx2	
<ul style="list-style-type: none">• Axtel Libre	

e) Our Markets

We provide local, long distance, data, internet, integrated solutions and value-added communications services in 27 of the largest metropolitan areas in the country, including Mexico City, Monterrey, Guadalajara, Puebla, Toluca, León, Querétaro, San Luis Potosí, Saltillo, Aguascalientes, Ciudad Juárez, Tijuana, Torreón (Laguna Region), Veracruz, Chihuahua, Celaya, Irapuato, Ciudad Victoria, Reynosa, Tampico, Cuernavaca, Mérida, Morelia, Pachuca, Hermosillo, San Juan del Rio and Xalapa. These 27 cities represent more than 44% of the total population of Mexico according to INEGI. With our long-haul network we also provide long-distance services in 200 cities in Mexico. We estimate that the cities in which we operate locally represent the majority of the total Mexican telecommunications revenue opportunity.

Our city roll-out is determined taking into consideration the following criteria:

- *Size of telecommunications opportunity.* According to COFETEL, for the year ended December 31, 2007, all net-additional lines in Mexico were concentrated in 12 of the 32 states: Chiapas, Chihuahua, Mexico City, Hidalgo, Michoacan, Nayarit, Oaxaca, Puebla, San Luis Potosi, Tamaulipas, Tlaxcala and Yucatan. Eleven of the 27 cities we currently serve are in these states and eight of them are state capitals.
- *Regional economy.* According to INEGI, in 2004, almost 85% of the total gross domestic product in Mexico was generated in the 18 states in which we have a local presence.
- *Operational synergies.* To become more efficient in launching cities, we decided to open clusters of cities to allow for quick systems and operations integration and network build-out.

Within these cities, studies were conducted using geographical, statistical and self-generated market research data to determine where the most attractive opportunities were concentrated. Our network has been built upon this comprehensive data allowing for fast penetration and cost-efficiency.

We believe that we have a 10.3% market share of our total addressable market in the 27 cities in which we offer local services. In Monterrey and Guadalajara, the first two markets where Axtel launched services, we estimate that we have achieved market shares, in each city, of approximately 16% and 14%. In particular, in the business market, we estimate that in Monterrey and Guadalajara we have achieved approximately a 17.4% and 17.8% market share, respectively. The table below provides our estimated market share as of December 31, 2007 for each of the cities where we offer local services, based on access lines.

**Market Share Within Coverage Market
As of December 31, 2007**

City	Date Launched	Res	Business	Total
Monterrey	Jun-99	16.1%	17.4%	16.5%
Guadalajara	Dec-99	12.3%	17.8%	13.8%
Mexico	Mar-00	7.2%	10.8%	8.3%
Puebla	Jan-01	8.4%	13.4%	9.6%
Toluca	Jan-01	8.8%	14.2%	9.8%
Leon	Jan-01	11.6%	20.5%	13.8%
Queretaro	Jul-04	9.8%	11.2%	10.3%
San Luis Potosi	Jul-04	16.8%	21.1%	17.8%
Aguascalientes	Oct-04	12.8%	7.7%	10.9%

Saltillo	Oct-04	10.9%	13.0%	11.4%
Ciudad Juarez	Nov-04	8.1%	7.0%	7.8%
Tijuana	Nov-04	20.4%	6.5%	15.7%
Torreon	Feb-06	7.8%	9.2%	8.1%
Veracruz	Feb-06	11.9%	14.6%	12.4%
Chihuahua	Mar-06	8.6%	6.6%	8.0%
Celaya	May-06	9.3%	8.7%	9.1%
Irapuato	Aug-06	7.0%	3.5%	6.2%
Cuernavaca	Mar-07	9.6%	7.3%	9.1%
Tampico	Mar-07	13.9%	6.9%	11.9%
Morelia	May-07	9.4%	10.1%	9.5%
Xalapa	Jun-07	11.5%	7.1%	10.6%
Mérida	Jun-07	6.1%	3.0%	5.2%
Hermosillo	Ago-07	5.3%	2.1%	4.4%
Reynosa	Oct-07	2.6%	0.4%	2.0%
Cd. Victoria	Oct-07	4.0%	0.8%	3.3%
Pachuca	Oct-07	1.8%	0.9%	1.6%
SJ del Río	Oct-07	3.4%	0.9%	2.8%
TOTAL		9.6%	11.8%	10.3%

Source: Market share percentages are company estimates based on number of lines in service divided by the average teledensity per square kilometer of coverage for each one of our radiobases.

Banamex, and its Mexican affiliates, Verizon Communications (formerly MCI) and Nextel de Mexico represent 19% of our total revenues as of December 31, 2007. We signed a five-year contract with Banamex on November 30, 2006, renewable for another five years, to provide products and services for all their telecommunications needs in existing and new operations. Verizon Communications provides us a significant volume of international traffic to terminate in Mexico, representing 2% of our total revenues for 2007. We have maintained this relationship with Verizon Communications since 1995. Nextel de Mexico provides telecommunications services to its customers through access to our network. We first entered into a services agreement with Nextel de Mexico in April 2001, and this agreement has been extended seven times. Pursuant to this business relationship, we extended the agreement until August 31, 2011 to continue providing Nextel de Mexico with local services, spectrum, long distance calling and 01-800 numbers, and other services, in a significant number of Mexican cities. Under this extension, we are guaranteed certain minimum levels of traffic every year until the expiration of the agreement.

Our telecommunications business is susceptible to seasonality, where our volume related revenues are impacted due to lower consumption levels in vacation and holiday periods. We estimate that about 40% to 50% of our revenues are volume related.

f) Marketing and Sales

Our marketing strategy is to position ourselves as the first and best alternative provider of local, long distance, internet, data and value-added integrated telecommunications services in Mexico. We undertake direct mail marketing (both special delivery and bill inserts) as well as telemarketing in order to generate geographically targeted brand awareness and to up-sell new services to existing customers. We also build brand awareness through the use of outdoor advertising and billboards, printed media including newspapers and magazines, advertisements on the radio and television and sponsorships of local news programs and co-sponsorship of programs with important companies in Mexico. Our brand strategy is to convey a modern, attractive image using simple, visual communication and portraying a human profile.

For corporate customers, financial institutions and federal government entities, we launched “*AXTEL Corporativos*”, a marketing initiative to strengthen our position as a unified communications supplier with a broad

range of administered solutions that allow large customers to increase the efficiency of their communications by converging different services. This group is responsible for all sales activities, contract negotiations and proactive account management.

We complement this marketing campaign with focused sales efforts directed to our target market using a variety of sales channels. Our primary sales methods are: direct sales; door to door sales; telemarketing; sales booths in strategically determined areas, including department stores, where potential customers carry out their shopping activities; MAPs (“*Módulos de Atención y Pago*”) which are Axtel-branded sales and service offices located at strategic locations within our targeted cities; and, sales distributors who are certified to carry out sales activities on our behalf and target specific niches.

Sales efficiency is measured by subscriber acquisition cost. Telemarketing has proven to be a highly efficient sales channel due to the quality of our detailed database systems, which screen potential customers based on geographic location, network availability and expressed interest. By effectively pre-selecting customers based on network availability, we are able to maximize telemarketing sales efficiency and decrease the cost of acquisition. The accuracy of our databases also results in highly efficient installations.

Customer churn occurs primarily from our disconnecting customers for non-payment of bills. Churn also occurs when a customer chooses to switch to a competing service or to terminate service altogether. Churn results in the loss of future revenue from customers whose service is disconnected and limits our ability to recoup costs incurred in acquiring customers such as switching costs, commissions and installation costs. Our average monthly churn rate for year 2007 was 1.3% vs. 1.4% recorded in the twelve months ended in December 31, 2006.

g) Pricing

In the residential market, in order to attract new subscribers, we actively promote attractive packages or bundles, which generate recurring monthly payments, like *Axtel Libre*, which offers unlimited local calling to mass market customers, or *Axtel in a Box*, a set of commercial packages we offer including local calling, minutes of long-distance and cellular and Internet access, under a single service at attractive prices for customers. Once a customer has chosen our services, we focus on customer satisfaction and offer the customer benefits, rather than lower pricing, in order to maximize our retention rate. For instance, under *Axtel x 2* we install and activate second lines for a small charge and allow customers free service trials for value-added services. In the business market, we attract users by offering a wide variety of advanced telecommunications services, like VPNs, dedicated private lines, co-location and network monitoring, in addition to voice services, which differentiate us from most of our competitors. For voice products, we offer volume discounts on local calls and provide additional services and discounts to customers who sign long-term contracts. To date, this strategy has allowed us to capture significant market share without eroding the value of the market through excessive price competition.

We maintain our prices at market levels. We offer pricing plans that are simple in order to assure customers of the integrity of the billing process. Our pricing structure rewards consumption by increasing discounts in relation to the amount billed. Our ability to introduce new products such as *Axtel in a Box*, or *Axtel Libre*, allows us to position ourselves as a value-added provider rather than competing on price only.

h) Our Network

We provide services using a complementary nationwide long-haul fiber-optic network with a hybrid wireline and fixed wireless local access network designed to optimize capital expenditures through the deployment of network access equipment based on specific customer requirements. Our last-mile access options include fixed wireless access, Symmetry, WiMAX, point-to-point and point-to-multipoint wireless technologies, as well as metropolitan fiber rings. We switch our traffic using DMS equipment that interconnects with Telmex’s equipment and that of other local and long distance carriers in each city where we provide local service.

Our wireless network uses customer access equipment, microwave radios, DMS switching and other equipment supplied by various vendors, including Motorola, Airspan, SR Telecom, Nortel Networks and Siemens, among

others. Our internet platform uses Cisco's routing platform with Compaq servers and Microsoft software applications. Our metropolitan fiber networks use Lucent Technology Allwave fiber and Nortel Networks DNX SDH equipment. The combination of these network components enables us to deliver world-class network reliability and service to our customers.

Through our current use of fixed wireless access technology, including Symmetry technology and WiMAX, we are able to provide our customers quality voice service and up to 4 Mbps data speeds.. Currently, we provide voice and data packages to mass market customers with Internet speed access from 256 kbps up to 4 mbps. We consider fixed wireless access technology to be ideal for our residential and micro and small business customers. Internet fixed wireless access technology, provides our customers with always-on data connections by using an internet protocol interface and dynamic timeslot assignments, which improves the data rates experienced by customers and also increases our network efficiency.

Basic voice and data services are delivered over all of our access technologies. Advanced data services and internet access with data rates ranging from 64 Kbps to 2,048 Kbps require deployment of additional equipment to support the customer's requirements. In general, the capabilities of the access technologies increase directly with the cost of the solution. Our hybrid access capability enables us to:

- provide a full range of voice, data and internet services;
- rapidly meet demand;
- penetrate specific target markets; and
- scale the infrastructure deployed to market demand and individual customer requirements.

This network infrastructure allows us to satisfy the requirements of diverse components of the market while maintaining a low-cost position relative to our competition.

Build-out strategy

Our local network has generally been built on a modular basis. Once a region of opportunity has been identified and the decision to expand has been made, we build our network in tandem with our sales efforts within the region. This approach provides greater flexibility and minimizes the time lag between the incurrence of capital expenditures and the generation of service revenues. This model differs significantly from a traditional wireline network covering the same geographic area in which the vast majority of capital expenditures are incurred prior to obtaining customer subscriptions.

Last-mile connectivity

The last-mile connectivity portion of our network is comprised of a mix of wireless technologies as well as fiber optics for customers within our metropolitan fiber optics rings. Our access technology is determined by cost-effectiveness analysis, customer applications and availability of service. We use fixed wireless access to serve customers requiring between one and nine lines of plain old telephony service ("POTS") in a single point of service. Point-to-multipoint is used for customers that require between 10 and 30 POTS and/or require low-speed (below 2,048 Kbps) dedicated private line accesses. Our point-to-point and fiber optics accesses are used for customers requiring digital trunks or dedicated private line accesses of more than 2Mbps. Hybrid solutions are being used in order to reach more customers by expanding service using digital loop concentrator and multi-tenant solutions.

We have contracts with Telefónica Data de México, a subsidiary of Telefónica de España, pursuant to which we acquired the right to use capacity in Telefonica's long haul fiber infrastructure which is located between the northern border of Mexico and Mexico City. Pursuant to such contracts, Telefónica Data de México has the right to

use a pair of dark fibers in a portion of our metropolitan fiber rings. We also maintain a similar agreement with Telereunión to use approximately 620 kilometers of long-distance fiber optic network in the Gulf of Mexico region.

Local Network

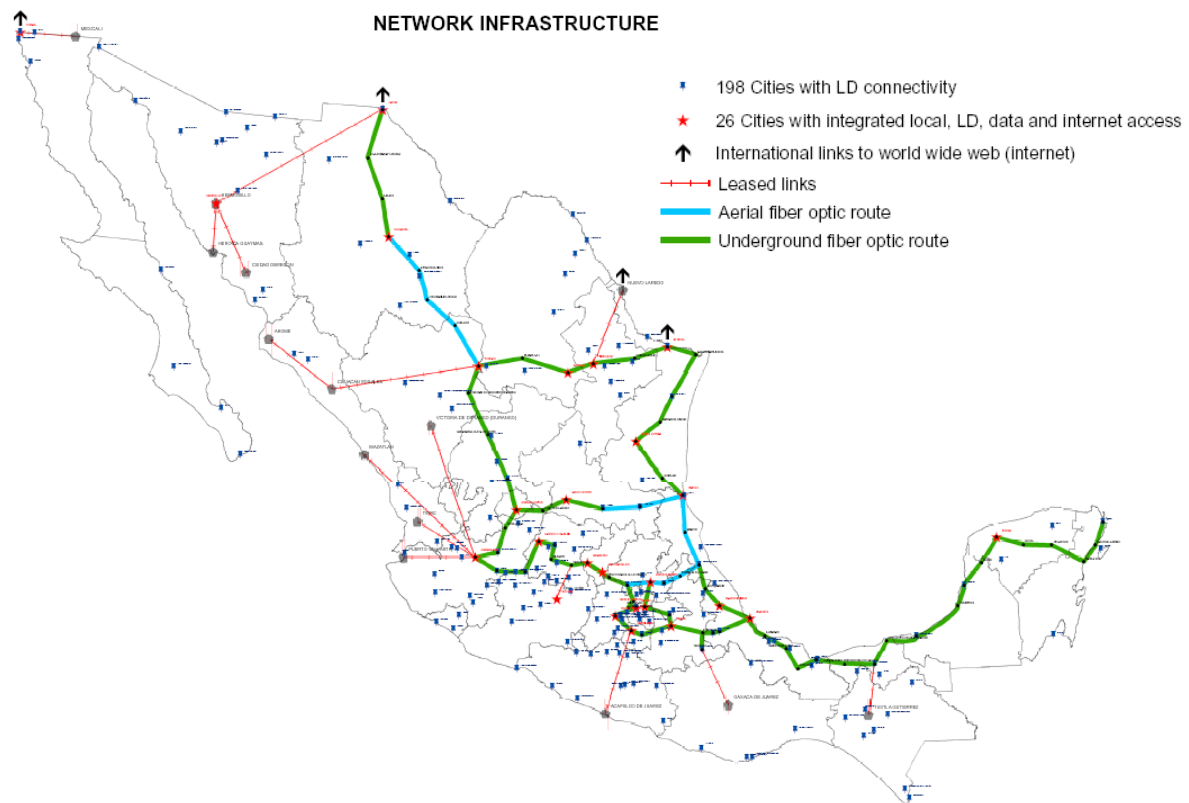
As of December 31, 2007, our metropolitan fiber optic rings totaled 1,366 kilometers in the cities where we offer local services. Our local network is comprised of several technologies, including fixed wireless access, WiMAX, copper, point-to-point, point-to-multipoint and fiber optic links.

The following summarizes our local infrastructure as of December 31, 2007:

City	FWA	Symmetry	WiMAX	PMP Sites	PTP Links	Switches	Metro Fiber Rings (Kms)
Monterrey	64	18	4	29	270	7	349
Guadalajara	63	8	19	23	231	5	145
Mexico	159	29		55	567	11	498
Puebla	20	3		7	79	1	70
Toluca	9	3		3	58	1	15
Leon	13	5		6	45	1	36
Queretaro	8	6		6	41	0	1
San Luis Potosi	11	5		5	16	0	22
Saltillo	7	4		4	31	0	37
Aguascalientes	9	5		4	15	0	9
Cd. Juarez	10	4		6	29	1	25
Tijuana	9	0		6	16	2	5
Torreon	7	5		3	34	1	6
Veracruz	6	5		4	16	1	24
Chihuahua	8	5		6	23	1	9
Celaya	2	3		2	13	0	10
Irapuato	0	3		1	0	0	19
Cuernavaca	5	2		3	16	0	5
Tampico	5	3		3	24	0	11
Morelia	4	4		2	4	2	3
Merida	4	3		2	21	1	16
Xalapa	3	3		1	1	0	5
Hermosillo	5	3		3	1	2	1
Others	0	14	0	6	4	0	45
Total	431	143	23	190	1,555	37	1,366

Long Distance Network

Our long distance fiber-optic network is 7,700 kilometers in length using “non-zero dispersion shifted” fiber-optic and underground and optical-ground wire cable, which supports SDH and Dense Wavelength Division Multiplexing (“DWDM”) technology. SDH enables the deployment of bi-directional ring architecture, a system that allows for nearly instantaneous re-routing of traffic in the event of an equipment failure or a fiber-optic cut. DWDM technology enables expanded transmission capacity over the same physical infrastructure through the installation of additional electronics. Our long distance network connects 49 cities through owned infrastructure, and 154 additional cities through leased infrastructure.



Switching

We use Nortel's DMS-100 digital switches to route traffic in twelve cities and Nortel's Call Server 2000 Softswitch to route traffic in five additional cities. We have four Nortel DMS-250 digital switches for long distance services are installed in the Main Switches Facilities to receive the traffic from more than 200 cities and international traffic from US and ROW. We have four Ericsson TL4 digital switches for local services, two located in Mexico, one in Monterrey and one in Guadalajara covering 16 cities. We use our A5020 Alcatel Softswitch used for Netvoice services and Internet Dialup. We have two SoftX3000 Huawei Softswitches that provide local services in eight cities and all the International VoIP traffic.

Our DMS-100 switches are capable of handling approximately up to 100,000 lines and the CS 2000 softswitches can handle up to 160,000, using the current software release. Both of these systems work on a modular basis and provide analog lines, E1 digital lines, digital high-speed data services, centrex services and operator assisted services. In addition, the CS2000 Softswitch can also provide multimedia capabilities by supporting multiple next generation protocols. Both switches can also provide private clear-channel digital lines, data transmission and value-added services such as four digit dialing, conference, call back, caller ID, call waiting, hot line and hunt group.

i) Operational Support Systems

We have an information technology architecture that is based upon Siebel, a customer relationship management system, SAP software for enterprise resource planning, CSG Systems International software for billing and Net Boss, an advanced network management system. These systems enable us to perform on-line sales and service provisioning. We have been able to manage customer requests, generate accurate bills and produce timely financial statements. These systems allow us to respond to customer requests with speed, quality and accuracy.

j) Our Concessions

We believe we have purchased sufficient spectrum to fulfill the capacity requirements of our business plan including the offering of broadband services to our customers. In September 1995, Avantel obtained a concession to offer local and long distance telephony services nationwide. In June 1996, Axtel also obtained a concession to offer local and long distance telephony services. Both concessions have a term of 30 years and, subject to the satisfaction of certain conditions, are renewable for an additional 30-year period.

We also hold concessions to use and exploit the following frequency bands:

- Two 929 MHz for radio messaging services;
- 50 MHz at 3.4 GHz, nationwide, divided into 9 regions for local telephony using fixed wireless access technology;
- 56 MHz at 7 GHz, nationwide, for long-haul point-to-point transport (a 50/50 ownership with Alestra);
- 60 MHz at 10.5 GHz, nationwide, for point-to-multipoint access;
- 120 MHz at 10.5 GHz, in 3 regions, for point-to-multipoint access;
- 168 MHz at 15 GHz, nationwide, for point-to-point access and transport;
- 368 MHz at 23 GHz, nationwide, for point-to-point access and transport; and
- 112 MHz at 37 to 38.6 GHz, in 5 regions, for point-to-point transport.

Each of the spectrum licenses has a term of 20 years and may be renewed at our option for additional 20-year periods as long as we are in compliance with all of our obligations thereunder and with any new conditions imposed in accordance with the law and as long as an agreement is reached on any new conditions set forth by the SCT.

The concession expressly permits us to provide the following services:

- basic local telephony;
- nationwide long distance telephony;
- the sale or lease of network capacity for the generation, transmission or reception of signs, signals, writings, images, voice, sounds or other information of any nature;
- the purchase and lease of network capacity from other carriers, including the lease of digital circuits;
- value-added services;
- operator services;
- data, video, audio and video conference services, except for cable or other restricted television, continuous music or digital audio services;
- credit or debit telephone cards; and
- public telephony services.

In November 2006, SCT granted, as part of Axtel's concession, a new permit to provide short message services ("SMS") to our clients.

We have the required regulatory authority to provide such services to Mexico's entire population. Some of our concessions require us to offer services in certain geographic areas where we are not currently offering services. With respect to those geographical areas in which we were required to provide such services by December 2007, we have complied with such coverage requirements. With respect to those geographical areas in which we are required to provide such services by December 2008, we expect to comply with such requirements as requested; however, if needed we may request the necessary extensions from the SCT in order to comply with the coverage requirements. If we do not receive the necessary extensions when requested, the SCT could revoke the specific permits and concessions covering such territories in which we do not provide services. In the past we have been able to obtain extensions from the SCT in order to comply with such requirements and have been able to maintain in full force in effect our permits and concessions. However, in the event that we were to lose our concessions for these areas where we do not presently offer our services, our concessions for the geographic areas where we do presently offer our services would not be adversely affected.

k) Interconnection

In accordance with the Federal Telecommunications Law, all holders of concessions for the installation, operation and exploitation of public telecommunications networks are required to provide interconnection services to other holders of public telecommunications network concessions.

All terms of interconnection (such as point of interconnection and interconnection fees) are negotiated between telecommunications concessionaires under COFETEL's supervision. Telecommunications concessionaires are prohibited from adopting discriminatory practices in the application of rates or any other terms of interconnection.

Agreements are typically signed for one-year periods. When agreements are renewed, parties can renegotiate new terms and conditions such as rates, technical aspects and minimum level of service conditions. If the parties do not come to an agreement, the previous existing conditions remain in place under an automatic extension until the parties reach a new agreement, maintaining the same rights and obligations until the new agreement is formalized. Parties can request that COFETEL intervene to resolve the conditions that cannot be agreed upon. By law, parties cannot cease to provide interconnection services to other carriers without a written authorization from SCT. In accordance with Mexican Telecommunications Regulations, we have established interconnection agreements depending on the type of traffic, as follows:

Local interconnection

Local interconnection agreements are established between two local fixed telephony providers in order to exchange local calls between their networks. Local interconnection agreements include provisions concerning local switched and non-switched interconnection, signaling, co-location and local transiting, among others.

The two most important conditions in local interconnection agreements are the per-minute interconnection fee and the "bill and keep" agreement. The current interconnection fee is US\$0.00975 per minute. We currently have two interconnection agreements with Telmex; one between Axtel and Telmex and another between Avantel and Telmex. The major differences among these agreements are the expiration date and the exception elements for the imbalance calculation. The imbalance threshold under the bill and keep agreement refers to the difference between the outgoing and the incoming local traffic of any carrier. If at any given month, this difference falls below the permitted threshold, there are no payments among the carriers. If any carrier surpasses the threshold, payments have to be made between carriers for the full amount of the imbalance. The bill and keep agreements contain exceptions regarding internet traffic, long duration calls, traffic generated by call centers, trunking operators and traffic generated by new customers (for a six month period) so that these exceptions will not affect the calculation of the permitted imbalance percentage.

Axtel and Telmex's agreement. Axtel entered into an interconnection agreement with Telmex in March of 1999. Axtel's interconnection agreement with Telmex expires on December 31, 2008. If the agreement expires without having been expressly extended by the parties, the agreement explicitly contemplates an automatic extension until both parties mutually agree to extend the expired agreement or execute a new interconnection agreement. The threshold for the differential between incoming and outgoing traffic set in this agreement is 5% and no payments have been made to Telmex since the implementation of this agreement.

Avantel and Telmex agreement. The Avantel interconnection agreement with Telmex was signed on October 1, 2006 and will expire on December 31, 2008. The threshold for the differential between incoming and outgoing traffic set in this agreement is 5%.

In addition to local interconnection agreements with Telmex, we have established interconnection agreements with most of the local fixed carriers, such as Teléfonos del Noroeste, S.A. de C.V. ("Telnor"), Alestra, Operadora Unefon, S.A. de C.V. ("Unefon") and Maxcom. The terms and conditions for each agreement are similar to those established with Telmex. Although we have no local interconnection agreement with Megacable Comunicaciones de Mexico, S.A. de C.V. due to particular legal issues between them and COFETEL, traffic is exchanged and interconnected between us and them through transit agreements with Telmex

Mobile interconnection

We have reciprocal interconnection agreements with all cellular providers (including Telcel, Unefon, Iusacell, Telefonica Movil, Cedetel, Norcel, Bajacel and Pegaso PCS) within each of the local coverage areas in which we operate. As of December 31, 2007, the wireline to mobile interconnection fee under the "calling party pays" mode payable to the cellular carriers was Ps. 1.34 per minute. In response to an administrative procedure we initiated against Telcel in 2005, the fixed to mobile interconnection fee payable to Telcel as of December 31, 2007 was Ps. 1.23 per minute, plus a 25% surcharge on the actual amount of minutes per month.

Long distance interconnection

Acting as local network. This interconnection agreement allows long distance carriers to deliver long distance calls from their users to our local network. It also allows our users to made calls to a non-geographic numbers (800s) assigned by COFETEL to such long distance carriers. We have long distance interconnection agreements in place with major long distance carriers such as LADA (Telmex and Telnor long distance operation) or Alestra, among others. Carriers that have not established this interconnection agreement with us, use traffic through LADA or other carrier that maintains an agreement in place with us. As of December 31, 2007, the interconnection fee we receive from long distance carriers was US\$0.01003 per minute (US\$0.00975 plus a surcharge of 2.085% per minute).

Acting as long distance network. These interconnection agreements, established with Telmex, Telnor and Maxcom, allow us to deliver long distance calls from our users to a local network. It also allows users of the local network to made calls to a non-geographic numbers (800s) assigned by COFETEL to us. It also allows users of Telmex or Telnor who have choose Avantel as their long distance carrier to use Avantel long distance services. As of December 31, 2007, the interconnection fee we pay to local carriers was US\$0.01003 per minute (US\$0.00975 plus a surcharge of 2.085% per minute).

Prices and tariffs charged under these long distance interconnection agreements are denominated in US dollars and then converted into Mexican pesos based on monthly exchange rates published by Banco de Mexico.

International settlement

Mexican carriers entitled to operate an international gateway do not have any restriction on the volume of international traffic that they can terminate in Mexico, as long as they comply with the Mexican telecommunications regulations.

In addition, each carrier is free to negotiate the applicable rates for international calls terminating in Mexico. Prior to application, rates must be registered with COFETEL.

l) Customer Service

A key element of our competitive strategy is to consistently provide reliable, responsive customer service. In order to achieve this goal, we have established a 24/7 customer service center for voice, data and internet services which is staffed by highly trained personnel. We have implemented a comprehensive training, testing and certification program for all staff that directly interacts with customers.

We provide post-sales service on a nationwide basis through the following:

- Customer Service provides post-sales customer support, ranging from general information, additions, moves and changes to billing inquiries and technical support.
- Operator Service is 24/7, providing directory assistance, wake-up calls, time of day, emergency calls and placing domestic and international long distance calls.
- Repair Answer is our customer contact group that addresses and manages all customer trouble reports and provides on-line technical support and analysis.
- Local Test analyzes and tests all trouble reports that are not resolved on-line by Repair Answer. This team is accountable for routing “in service” and “out of service” trouble reports to Repair Dispatch. Both Repair and Local Test work closely with our network maintenance center in order to monitor and fix network disruptions.

Additionally, with the acquisition of Avantel we added two National Management and Monitoring Centers located in Monterrey and Guadalajara.

m) Billing and Collection

We believe our billing and collection process is an important aspect of our competitive advantage.

Our billing team receives and validates the call detail record from the network and bills customers on a monthly basis, typically within 14 days from the end of the billing period. Bills are due typically 25 days from the end of the billing period for mass market customers, while carriers, corporate and government customers have extended periods.

An ongoing revenue assurance process, which consists of reviewing the billing stream, payments and adjustments, as well as fraud detection and control, has become part of our regular billing operation. This process has contributed to minimizing fraud and risk.

To facilitate the reception of payments and to make the payment process convenient for customers, we have developed a number of payment reception channels. Some of these channels are:

- convenience stores;
- banks;
- Axtel MAPs (Axtel’s Sales and Payment Points);
- e-billing;

- Internet;
- supermarkets;
- automatic charges to credit cards, checking and debit accounts (upon customer approval); and
- TELECOM (Mexico's mail and telegraph company) outlets for Avantel customers only.

These channels provide easy and fast options for customers to select the most suitable and convenient alternative for a prompt payment.

To encourage customers to pay on time, we use preventive tactics such as calls to remind customers that have failed to pay promptly on their previous payment due dates and call interception. Additional procedures involve suspension of long distance and cellular outgoing calling, suspension of outbound calling and total suspension of service.

Past due accounts are turned over to external collections agencies 90 days after their due date (except for government accounts). Accounts are disconnected 180 days after their due date. Prior to disconnection, we conduct a negotiation of the outstanding balance with the customer as part of our retention efforts oriented to provide alternate solutions payment programs. Alternatives include reconnection of the service under a pre-payment scheme with a payment schedule for the outstanding balance.

n) Competition

We compete primarily in the local telephony services market on the basis of features, customer service and value. Our direct competitors are wireline and fixed wireless local telephony operators. We also compete directly in the long distance market and we now provide long distance services separately from our local telephony service.

We believe there may be additional opportunities for consolidation in the Mexican telecommunications industry. Although it is not our main strategy, we intend to review and evaluate opportunities from time to time and, if an appropriate opportunity arises, we may pursue it through the strategic acquisition of assets or an acquisition of, or combination with, another company.

Telmex. Our main local telephony competitor is Telmex, the former state-owned telecommunications monopoly. Telmex has significantly greater financial and other resources than we have and serves all of the cities and markets that we serve. In addition, Telmex has an established customer base which represents the vast majority of the wireline local telephony lines in Mexico.

Telmex is the dominant provider of local telephony services and, as such, a significant number of our customers maintain an ongoing relationship with Telmex. Telmex has a presence throughout Mexico and its established and long-standing customer base gives it a substantial competitive advantage. See Item 3.D "Risk Factors—Risks Relating to Our Company—We depend on Telmex for interconnection and we may be forced to pay higher interconnection fees in the future, which could have a material adverse effect on our business and results of operations."

With the convergence legislation enacted in 2006, Telmex will be able to provide video subject to obtaining the modification of its concession and complying with certain other obligations. Telmex's significant customer base provides significant leverage to develop the triple play services (voice, Internet and video) demand significantly. Telmex has publicly stated its intentions to offer triple-play services in the near future.

Alestra. Alestra commenced operations in 1996, providing only long distance telephony services to residential and business customers. In 2000, Alestra also started to offer local services to corporate customers in Mexico, Monterrey and Guadalajara, primarily. According to their 2007 20-F Report, Alestra is owned 49% by AT&T Telecom Mexico, Inc., a wholly owned subsidiary of AT&T Inc. and 51% by Onexa, S.A. de C.V., a

corporation owned by Alfa, S.A.B. de C.V. Their network consists of 5,017 kilometers of long-distance fiber and 1,084 kilometers of metropolitan rings. Due to the acquisition by the former SBC Communications Inc. of the former AT&T Corp., AT&T Inc. acquired certain obligations and restrictions with Alestra concerning direct competition and mandatory net margin contribution, among others, due to the significant ownership that the former SBC Communications Inc., now AT&T Inc., maintain in Telmex.

Maxcom. Maxcom commenced operations in 1999 targeting, initially, residential and small business customers in the cities of Puebla, Mexico City and Querétaro. More recently, through joint-venture agreements with other companies, they have added a small presence in the cities of Guadalajara, Monterrey, Toluca and San Luis. Maxcom has deployed a wireline network in these cities and after eight years of operations, its customer base has grown to approximately 360,942 “revenue generating units” as of December 31, 2007.

Cable Companies. By virtue of the convergence legislation issued by COFETEL in October 2006, we expect that starting next year the most important cable companies in Mexico will start providing local telephone services to residential and small business customers in Mexico’s major cities, including many where we have operations.

Other. The legislative initiatives passed in 2006 created a legal framework for broadcasting companies to eventually provide voice and data services.

o) Legal Proceedings

We are currently party to the following material legal proceedings:

Metronet Dispute

In October 2002, Metronet, S.A. de C.V. (“Metronet”) filed an action against us in the Fourth Civil Court in Monterrey (Mexico). Metronet claimed that we wrongfully terminated a letter of intent seeking payment for services and direct damages of approximately US\$3.8 million, plus other expenses and attorneys’ fees. On December 14, 2007, the parties reached an agreement and settled the dispute on definitive terms.

Spectrasite Dispute

In March 2002, Spectrasite Communications Mexico, S. de R.L. de C.V. (“Spectrasite Mexico”) filed an action against us in the 30th Civil Court in Mexico City. Spectrasite Mexico is seeking recovery of a deposit in the amount of US\$13.0 million that Spectrasite Mexico made with us in connection with a proposed sale-leaseback of towers. We, in turn, countersued Spectrasite Mexico and Spectrasite Communications Inc. for breach of contract in a related action. If the court rules against us, the deposit will have to be reimbursed as will Spectrasite Mexico’s legal costs and expenses and any other applicable amounts considered direct damages in accordance with applicable Mexican laws. If the court rules in our favor, we may be able to retain the deposit and/or any other applicable amounts considered as direct damages in accordance with applicable Mexican laws, in addition to receiving payment of our legal costs and expenses. On December 15, 2004, Spectrasite Communications Inc. was duly served. On April 1, 2008, the trial court ruled against us ordering Axtel to return the deposit and applicable interests. The Company will appeal the trial court’s order before the Superior Court of Appeal.

Global Link Dispute

On November 28, 2002, Global Link Telecom Corporation (“Global Link”) requested a payment of one million US dollars from Avantel due to the fact that Global Link filed voluntary petition for reorganization under Chapter 11 of the US Bankruptcy Code. This amount relates to payments made by Global Telecommunications Solutions de Mexico, S. de R.L. de C.V. 90 days before the Global Link reorganization period began. In October 2003, the bankruptcy committee in charge of this case increased the requested amount to three million US dollars. On July 12, 2007, the parties reached an agreement and settled the dispute on definitive terms.

p) Regulatory Proceedings

In April 2006, COFETEL issued new general rules for the obligation to implement, on a national level, the system named “Calling Party Pays”. Under the new legal framework the interconnection fees for national and international long distance calls will be increased. Axtel and Avantel have challenged such new legal framework in the administrative and judicial courts of Mexico. These proceedings have not yet been resolved, and we cannot determine with reasonable certainty the impact these proceedings would have if they are not resolved in our favor.

In August 2006, COFETEL resolved interconnection disputes between Telcel and Avantel. In this resolution COFETEL approved a reduction of the interconnection fees to be paid by Avantel for calls terminated in Telcel’s network for the years between 2005 and 2010. Telcel challenged this resolution. These proceedings have not yet been resolved, and we cannot determine with reasonable certainty the impact that these proceedings may have if they are not resolved in Avantel’s favor.

In August 2006, COFETEL resolved interconnection disputes between us and Telcel. In this resolution COFETEL approved a reduction of the interconnection fees to be paid by us for calls terminated in Telcel’s network for the years between 2005 and 2010. Telcel challenged this resolution. This proceeding has been resolved confirming the reduced interconnection tariffs for the years between 2005 and 2007. The new resolution has been challenged by us and also by Telcel, and we cannot determine with reasonable certainty the impact that these proceedings may have if they are not resolved in our favor. In addition, we have started new administrative proceedings before COFETEL in order to obtain new interconnection tariffs for the years between 2008 and 2011.

In addition to the foregoing, on May 2007 COFETEL resolved other interconnection disputes initiated by us against the remaining cellular telephone companies. COFETEL approved a reduction of the interconnection fees with respect to such cellular telephone companies. We challenged this resolution. These proceedings have not been resolved and we cannot determine with reasonable certainty the impact that these proceedings may have if they are not resolved in our favor.

In December 2005, COFETEL determined the proportion of call attempts that each of the operators with an international port has the right to collect with respect to 1999 through 2004. Avantel challenged this resolution by initiating various administrative procedures. These proceedings have not yet been resolved, and we cannot determine with reasonable certainty the impact these proceedings would have if they are not resolved in our favor.

q) Environmental, Health and Safety Matters

We are subject to laws and regulations relating to the protection of the environment and human health and safety, including those governing the management and disposal of hazardous substances and wastes and the cleanup of contamination. As an owner or operator of property and in connection with the current or historical use of hazardous substances at our sites, we could incur costs, including cleanup costs, fines and third-party claims, as a result of violations of or liabilities under environmental or health and safety laws and regulations. We believe, however, that our operations are in substantial compliance with all such laws and regulations.

r) Enforceability of Civil Liabilities Against Foreign Persons

We and our subsidiaries (except for one subsidiary organized in the United States) are either variable capital corporations (*sociedades anónimas de capital variable*), limited liability companies (*sociedades de responsabilidad limitada de capital variable*) or fixed capital corporations (*sociedades anónimas*) (organized under the laws of Mexico, and are headquartered, managed and operated outside of the United States (principally in Mexico). Most of our directors and all of our officers reside in Mexico. All or a substantial portion of our assets and the assets of most of our directors and all of our officers are located outside of the United States (principally in Mexico). As a result, it may not be possible for investors or our shareholders to effect service of process outside of Mexico or within the United States upon us or such persons, or to enforce a judgment obtained in the United States against us or them outside of Mexico or in the United States courts that is based on the civil liability provisions under laws of jurisdictions other than Mexico including the federal and state securities laws or other laws of the United States.

We have been advised by our special Mexican counsel, D&A Morales y Asociados, S.C., that no treaty is in effect between the United States and Mexico calling for the mutual recognition and enforcement of their respective judgments. The recognition by Mexican courts of a judgment rendered in the United States is usually done under the principle of reciprocity, which means that Mexican courts would reexamine judgments rendered in the United States if such foreign country would reexamine Mexican judgments. Mexican courts may enforce judgments rendered in the United States through a homologation procedure consisting of the review by such Mexican courts of the foreign judgment to ascertain whether certain requirements of due process, reciprocity and public policy have been complied with, without reviewing the merits of the subject matter of the case. A judgment rendered in the United States may or need not be recognized if, among others:

- the foreign court did not have jurisdiction over the subject matter in a manner that is compatible with or analogous to Mexican laws or the subject matter is within the exclusive jurisdiction of Mexican courts;
- the judgment was rendered under a system which does not provide procedures compatible with due process requirements;
- enforcement of the judgment would be contrary to public policy of Mexico or generally accepted principles of international law;
- the defendant did not receive adequate personal notice in sufficient time to defend itself;
- the judgment is not final in the rendering state;
- the judgment conflicts with another final judgment; or
- the court of the rendering state would not enforce Mexican judgments as a matter of reciprocity.

Furthermore, there is doubt as to the enforceability, in actions originated in Mexico, of liabilities based in whole or in part on the United States federal or state securities laws, and as to the enforceability of judgments obtained in the United States in actions based in whole or in part on the civil liability provisions of United States federal or state securities laws.

s) Current Regulatory Environment

General

The telecommunications industry in Mexico is subject to the Federal Telecommunications Law and its regulations. In addition, certain rules under the General Means of Communications Law (*Ley de Vías Generales de Comunicación*) and the Telecommunications Regulations (*Reglamento de Telecomunicaciones*) generally remain effective.

Under the Federal Telecommunications Law, the Mexican telecommunications industry is regulated for regulatory, administrative and operational matters by COFETEL. COFETEL was created in 1996 as a separate entity from the SCT to regulate and promote the efficient development of the telecommunications industry in Mexico. COFETEL is responsible for, among other things:

- enacting regulations and technical standards for the telecommunications industry;
- ensuring that concession holders fulfill the terms and obligations of their concessions and permits;
- suspending operators without concessions;

- resolving interconnection controversies between competitors; and
- maintaining a registry of applicable rates.

The SCT retains the authority to grant and revoke all concessions and permits. COFETEL makes recommendations to the SCT on major issues, such as amending existing telecommunications legal framework, allocating spectrum frequencies, granting, transferring, renewing or revoking concessions and applying penalties for concession violations. The SCT has final decision making power on these issues. Once a final decision is made, COFETEL implements the related regulations.

Concessions and permits

To provide telephony services in Mexico through a public telecommunications network, a service provider must first obtain a concession from the SCT. Pursuant to the Federal Telecommunications Law, concessions for public telecommunications networks may not exceed a term of 30 years, and concessions for spectrum frequencies may not exceed a term of 20 years. Generally, concessions for public telecommunications networks and spectrum frequencies may be extended for a term equivalent to the term for which the concessions were originally granted as long as the concessionaire is in compliance with ongoing obligations stated therein. Concessions specify, among other things:

the type and technical specifications of the network, system or telecommunication services that may be provided;

- the allocated spectrum frequencies, if applicable;
- the geographical region in which the holder of the concession may provide the telecommunication service;
- the required capital expenditure program;
- the term during which such service may be provided;
- the payment, where applicable, required to be made to acquire the concession, including, if applicable, the participation of the Mexican government in the revenues of the holder of the concession; and
- any other rights and obligations affecting the concession holder.

In addition to concessions, the SCT may also grant permits for the following:

- installing, operating or exploiting transmission-ground stations; and
- providing telecommunications services as a reseller.

There is no legally mandated maximum term for these permits unless specifically stated in the permit. Under the Federal Telecommunications Law, a company needs to register with COFETEL the rates for the telecommunications services that it wishes to provide in order to be able to provide them to the public.

On March 31, 2006, the Mexican Federal Congress approved certain amendments to the Federal Television and Radio Law and the Telecommunication Law, which contains certain modifications to the legal framework of the broadcasting and telecommunications industries.

In October 2006 the SCT issued a new convergence program by which the concessionaires of telephony services are allowed to provide restricted television and audio services and the concessionaires of restricted

television and audio services are allowed to provide telephony services as long as the concessionaries adhere and accept the program's terms, which include among others, the obligation to allow telephone number portability.

Ownership restrictions. Under the Federal Telecommunications Law and the Mexican Foreign Investment Law (*Ley Federal de Inversión Extranjera*), basic telephony concessions may be granted only to:

- Mexican individuals; and
- Mexican corporations in which non-Mexicans own 49% or less of the full voting stock and that are not otherwise controlled by non-Mexicans.

However, in the case of concessions for cellular telecommunications services, foreign investment participation may exceed 49% of the voting stock with the prior approval of the Mexican Foreign Investment Bureau of the Mexican Ministry of Economy (*Secretaría de Economía*).

Pursuant to the Foreign Investment Law, the Mexican Ministry of Economy may also authorize the issuance of non-voting or limited-voting stock (also known as “neutral shares”) that are not counted for purposes of determining the foreign investment percentage of a Mexican corporation under the Mexican Foreign Investment Law. Any share transfers resulting in a violation of these foreign ownership requirements are invalid under Mexican law.

Transfer. Concessions are transferable after the first three-year period of the concession. If the SCT approves the transfer of the concession title, the assignee agrees to comply with the terms of the concession and such a transfer does not violate the foreign ownership requirements of the Federal Telecommunications Law and the Mexican Foreign Investment Law.

Termination. A concession or a permit may be terminated pursuant to the Federal Telecommunications Law upon the following events:

- expiration of its term;
- resignation by the concession holder or the permit holder;
- dissolution or bankruptcy of the concession holder or the permitholder; or
- revocation by SCT.

Revocation. A concession or a permit may be revoked pursuant to the Federal Telecommunications Law upon the following events:

- failure to exercise the rights of the concession within 180 days of its granting;
- failure to provide interconnection services with other holders of telecommunications concessions and permits without just cause;
- loss of the concession or permit holder's Mexican nationality;
- unauthorized assignment, transfer or encumbrance of the concession or permit;
- unauthorized interruption of service;
- taking any action that impairs the rights of other concessionaires or permit holders;

- failure to comply with the obligations or conditions specified in the concession or permit; and
- failure to pay the Mexican government its fee for the concession or, where applicable, its participation in the revenues of the holder of the concession.

The SCT may revoke a concession for violations in any of the circumstances referred to in the first four instances above. Under the last four instances above, the SCT would have to fine the concessionaire at least three times for the same failure before moving to revoke a concession.

Expropriation

The Mexican government has the statutory right to permanently expropriate any telecommunications concession and claim any related assets for reasons of public interest. Under Mexican law, the Mexican government is obligated to compensate the owner of such assets in the case of a statutory expropriation. The amount of the compensation is to be determined by appraisers. If the party affected by the expropriation disagrees with the appraisal amount, such party may initiate judicial action against the government. In such a case, the relevant judicial authority will determine the appropriate amount of compensation to be paid. We are not aware of any instance in which the SCT has exercised its expropriation rights in connection with a telecommunications company.

Temporary seizure

The Mexican government, through the SCT, may also temporarily seize all assets related to a telecommunications concession or permit in the event of a natural disaster, war, significant public disturbance, threats to internal peace or for economic reasons or for other reasons related to national security. If the Mexican government temporarily seizes such assets, except in the event of war, it must indemnify the concession holder for all losses and damages, including lost revenues. We are not aware of any instance in which the SCT has exercised its temporary seizure powers in connection with a fixed or mobile telecommunications company.

Rates for telecommunications services

Before the Federal Telecommunications Law was enacted, the SCT's approval was required for setting the rates charged for all basic local, long distance and certain value-added local and long distance telecommunications services. Historically, the SCT permitted rate increases based on the cost of service, the level of competition, the financial situation of the carrier and certain macroeconomic factors. Carriers were not allowed to discount the rates authorized by the SCT, although operators occasionally waived activation fees on a promotional basis. Interconnection rates also required SCT approval. Rates for private dedicated circuit services through microwave networks and private networks through satellites were not regulated before the Federal Telecommunications Law was enacted.

Under the Federal Telecommunications Law, rates for telecommunications services (including local, cellular and long distance telephony services) are now freely determined by the providers of such services, except that such rates may not be set below a service provider's long-term incremental cost.

In addition, COFETEL is authorized to impose specific rate, quality and service requirements on those companies determined by the Federal Antitrust Commission (*Comisión Federal de Competencia*) to have substantial market power pursuant to the provisions of Mexico's antitrust statute. All rates for telecommunications services (other than value-added services) must be registered with COFETEL prior to becoming effective. The Federal Telecommunications Law prohibits telecommunications providers from cross-subsidizing among their services and requires that they keep separate accounting for each of their services.

The Mexican Antitrust Commission has found that Telmex has substantial power in the following five markets: interconnection, local services, domestic long distance services, international long distance services and long distance resale, as defined under Mexico's antitrust statute. Based on this finding, COFETEL issued a resolution in September 2000 regulating Telmex as a dominant carrier and imposing special obligations regarding, among other

things, quality of services, tariffs and information disclosure. However, Telmex has obtained an injunction against any potential action by COFETEL for the purpose of implementing such resolution. As a result of this injunction, Telmex is not currently subject to the specific obligations covered by COFETEL's resolution.

Tax law

Income tax rate in Mexico is 28%. Mexican regulations allow companies to deduct tax losses against income tax, potentially reducing tax payments.

C. Organizational Structure

Axtel, S.A.B. de C.V. has the following direct or indirect ownership interest in the following Capital Stock (all but Telecom Networks Inc. are subsidiaries incorporated in Mexico):

- (i) 100% of the Capital Stock issued by AVANTEL, S. DE R.L. DE C.V.,
- (ii) 100% of the Capital Stock issued by AVANTEL INFRAESTRUCTURA, S. DE R.L. DE C.V.,
- (iii) 100% of the Capital Stock issued by INSTALACIONES Y CONTRATACIONES, S.A. DE C.V.,
- (iv) 100% of the Capital Stock issued by IMPULSORA E INMOBILIARIA REGIONAL, S.A. DE C.V.,
- (v) 100% of the Capital Stock issued by SERVICIOS AXTEL, S.A.B. DE C.V.,
- (vi) 100% of the Capital Stock issued by AVANTEL SERVICIOS, S.A. DE C.V.,
- (vii) 100% of the Capital Stock issued by AVANTEL RECURSOS, S.A. DE C.V.,
- (viii) 100% of the Capital Stock issued by AVANTEL EQUIPOS, S.A. DE C.V.,
- (ix) 100% of the Capital Stock issued by AVANTEL TELECOMUNICACIONES, S.A. DE C.V.,
- (x) 100% of the Capital Stock issued by ADEQUIP, S.A.,
- (xi) 100% of the Capital Stock issued by TELECOM NETWORKS INC. (incorporated in the U.S.A.), and
- (xii) 50% of the Capital Stock issued by CONECTIVIDAD INALÁMBRICA 7 GHZ, S.DE R.L.

D. Property, Plants and Equipment

All of our properties are located in Mexico. Our most important asset is our network infrastructure (See Item 4. Information on the Company, (h) Our Network).

Our corporate headquarters are located in Monterrey, Mexico. Our Monterrey office consists of 39,779 square meters. The lease on this property expires in 2015. We also own or lease office space and warehouses throughout the 27 cities where we operate. These are the facilities in which we have installed our switches and administrative offices. Office space or warehouses with more than 1,000 square meters are the following:

Name	Utilization/Use	Location	Area in m2	Property	Contract Ending Date
Headquarters Monterrey	Administrative	Monterrey	39,779	Lease	25/05/2015
Voice Center Apodaca	Operating Center	Monterrey	11,978	Lease	14/09/2005
Call Center	Operating Center	Santa Catarina	10,389	Lease	31/07/2011

Torre Axtel Santa Fe	Administrative	Mexico	10,259	Lease	01/01/2011
Workcenter Alse Blanco	Operating Center	Mexico	7,352	Lease	01/12/2011
Headquarters Axtel Reforma	Administrative	Mexico	6,150	Lease	28/02/2008
Switch 1	Technology Facility	Guadalajara	5,550	Owned	-
CIC Apodaca	Technology Facility	Monterrey	5,164	Lease	14/09/2005
Switch 2	Technology Facility	Mexico	3,434	Owned	-
Switch 1	Technology Facility	Monterrey	3,096	Owned	-
Workcenter San Jerónimo	Operating Center	Monterrey	3,093	Lease	03/03/2012
Switch y Workcenter	Operating and administrative center	Cd. Juarez	3,043	Owned	-
Offices	Administrative	Tampico	3,000	Lease	30/11/2011
CIC Puente	Technology Facility	Mexico	2,851	Owned	-
Switch 2	Technology Facility	Guadalajara	2,376	Owned	-
Switch 2	Technology Facility	Monterrey	2,111	Lease	30/03/2030
Offices and MAP	Administrative	Mérida	1,908	Lease	31/03/2010
Switch 1 y 3	Technology Facility	Mexico	1,898	Owned	-
Workcenter	Operating Center	Xalapa	1,724	Lease	30/10/2016
Workcenter	Operating Center	Leon	1,516	Owned	-
Workcenter	Operating Center	Tijuana	1,500	Lease	31/07/2007
Warehouse México	Operating Center	Mexico	1,500	Lease	01/05/2007
MSF Triunfo	Operating Center	Mexico	1,393	Owned	-
Systems Site Apodaca	Technology Facility	Monterrey	1,369	Leased	14/09/2005
Workcenter	Operating Center	Aguascalientes	1,200	Lease	14/06/2010
Workcenter	Operating Center	Reynosa	1,200	Lease	31/07/2010
Offices	Administrative	Puebla	1,193	Lease	30/09/2010
Warehouse Guadalupe	Operating Center	Monterrey	1,193	Lease	01/05/2006
Switch	Technology Facility	Toluca	1,188	Owned	-
POP Guadalupe	Technology Facility	Monterrey	1,140	Lease	01/10/2010
Offices, Administrative and MAP Admon. y Workcenter	Workcenter	Saltillo	1,100	Lease	31/05/2024
Oficinas y MAP	Administrative	Xalapa	1,100	Lease	27/02/2017
Switch	Technology Facility	Leon	1,099	Owned	-
Workcenter	Operating Center	Coatzacoalcos	1,061	Lease	31/12/2017
Workcenter	Operating Center	Veracruz	1,058	Lease	30/09/2011
Workcenter	Operating Center	Hermosillo	1,019	Lease	31/03/2010
Workcenter	Operating Center	Mérida	1,000	Lease	28/02/2009
Workcenter	Operating Center	Hidalgo	1,000	Lease	30/06/2010
Workcenter	Operating Center	Cd. Victoria	1,000	Lease	14/07/2010
Workcenter	Operating Center	Cuernavaca	1,000	Lease	14/10/2009
Workcenter	Operating Center	Culiacán	1,000	Lease	14/10/2010

Item 4.A UNRESOLVED STAFF COMMENTS

Not Applicable

Item 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following discussion should be read in conjunction with our financial statements and the notes thereto included elsewhere in this Form 20-F. The following discussion includes certain forward-looking statements. For a

discussion of important factors, including the continuing development of our business, actions of regulatory authorities and competitors and other factors which could cause actual results to differ materially from the results referred to in the forward-looking statements, see Item 3.D. “Risk Factors.”

A. Operating Results

a) Overview

We provide multiple voice, data and internet services bundled into integrated telecommunications solutions for businesses and high-usage residential customers. We also offer services to foreign carriers with international traffic termination, as well as providing custom-made integrated telecommunications services to large corporate customers. Our integrated service offering enables us to maximize the recurring revenue received from each customer, increasing the return achieved on our investment in infrastructure, sales and marketing and distribution. In addition, we believe that customers prefer to purchase their telecommunications services from a single provider and receive a single bill. We believe customer loyalty is increased with the provision of additional services, resulting in a lower customer churn rate.

b) Key performance indicators

Management evaluates the performance of the Company by tracking the following indicators:

	2005				2006				2007			
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
Revenues(1)	1,238.5	1,325.6	1,372.1	1,426.2	1,406.3	1,510.3	1,580.9	2,178.1	3,005.5	3,116.0	3,081.3	2,987.9
Local Service.....	854.3	933.9	966.6	1,015.9	998.7	1,065.7	1,108.0	1,157.6	1,278.8	1,326.1	1,337.5	1,394.3
Long Distance Services	111.7	123.7	128.3	124.2	113.5	129.9	133.8	206.5	402.7	419.4	352.3	357.7
Data	49.5	50.5	56.4	59.3	60.6	69.1	80.3	249.2	619.5	628.4	645.8	620.1
International traffic	134.6	124.4	124.3	126.0	118.6	125.4	121.4	187.4	293.0	330.4	313.9	272.9
Other Services	88.4	93.0	96.5	100.8	114.9	120.3	137.5	377.5	411.5	411.7	431.7	342.9
Cost of Revenues and Operating Expenses (1)	(831.5)	(865.0)	(880.6)	(918.6)	(896.8)	(973.2)	(1,025.4)	(1,469.0)	(2,070.8)	(2,054.7)	(1,995.2)	(1,985.4)
Access Lines (2)(3)(5)	490.2	529.7	567.2	605.9	648.4	697.0	733.1	792.5	815.2	843.7	884.6	932.3
Average Lines (2)(5)(6)	471.9	509.9	548.4	586.5	627.2	672.7	715.0	762.8	803.9	829.5	864.2	908.5
Monthly ARPU (4)(5)(7)	682.4	691.4	665.5	647.9	591.1	592.5	578.9	596.1	697.2	701.4	651.8	642.8
Customers (2)(3)(5)	307.9	327.7	347.5	368.2	394.0	422.0	444.6	502.4	518.0	543.8	576.0	623.2
Presubscription (LD) users (2)(3)(5)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	298.5	280.8	270.0	265.1	246.1

(1) Amounts in constant Ps. in millions as of December 31, 2007.

(2) Amounts in thousands.

(3) Figures as of the end of each period.

(4) Amounts in constant Ps. as of December 31, 2007.

(5) Unaudited information.

(6) Average Lines is the result of the Access Lines at the beginning of the period plus Access Lines at the end of the period divided by 2.

(7) Monthly ARPU is the result of the sum of local and long distance revenues divided with the Average Lines of the quarter divided by 3.

Revenues

We derive our revenues from:

- *Local calling services.* We generate revenue by enabling our customers to originate and receive an unlimited number of calls within a defined local service area. Customers are charged a flat

monthly fee for basic service, a per call fee for local calls (“measured service”), a per minute usage fee for calls completed on a cellular line (“calling party pays,” or CPP calls) and a monthly fee for value added services.

- *Long distance services.* We generate revenues by providing long distance services (domestic and international) for our customers’ completed calls.
- *Data & Network.* We generate revenues by providing data and network services, like Internet access, virtual private networks and private lines, to our customers.
- *International Traffic.* We generate revenues by terminating international traffic from foreign carriers in Mexico.
- *Other services.* We generate revenues from other services, which include, among others, activation fees for new customers, sale of customer premises equipments (“CPEs”) and revenues from integrated services billed to customers.

The following summarizes our revenues and percentage of revenues from operations from these sources:

Revenue Source	Revenues (1)				% of Revenues			
	Year ended December 31,				Year Ended December 31,			
	2004	2005	2006	2007	2004	2005	2006	2007
Local calling services.....	Ps. 3,002.5	Ps. 3,770.8	Ps. 4,330.0	Ps. 5,336.6	69.7%	70.3%	64.9%	43.8%
Long distance services	425.9	487.9	583.6	1,532.2	9.9%	9.1%	8.7%	12.6%
Data & Network	214.5	215.7	459.1	2,513.8	5.0%	4.0%	6.9%	20.6%
International Traffic	410.2	509.3	552.8	1,210.2	9.5%	9.5%	8.3%	9.9%
Other services.....	253.4	378.7	750.2	1,597.8	5.9%	7.1%	11.2%	13.1%
Total.....	Ps. 4,306.4	Ps. 5,362.4	Ps. 6,675.7	Ps. 12,190.6	100.0%	100.0%	100.0%	100.0%

(1) Amounts in constant Ps. in millions as of December 31, 2007.

Cost of Revenues and Operating Expenses

Our costs are categorized as follows:

- Cost of revenues include expenses related to the termination of our customers’ cellular and long distance calls in other carriers’ networks, as well as expenses related to billing, payment processing, operator services and our leasing of private circuit links.
- Operating expenses include costs incurred in connection with general and administrative matters including compensation and benefits, the costs of leasing land related to our operations and costs associated with sales and marketing and the maintenance of our network.
- Depreciation and amortization includes depreciation of all communications network and equipment and amortization of preoperating expenses and the cost of spectrum licenses.

Access Lines

Our access lines are separated into residential and business categories. We determine the number of our total access lines by adding to the ending balance of access lines from the previous period the gross installed access lines during such period and then subtracting any access lines that were disconnected during such period. By then determining the number of our access lines, we are able to estimate our share of that particular geographic market.

Average Revenue Per User (ARPU)

Average revenue per user is used as an industry-standard measurement of a telecommunications company's ability to maximize the amount of recurring revenues it derives from each customer in light of the amount of capital expenditures made to attract such customer. This measurement allows us to gauge our return on investment as compared with both our domestic competitors in Mexico as well as other telecommunication services providers abroad.

c) Year Over Year Comparisons

Year Ended December 31, 2007 Compared with Year Ended December 31, 2006

Revenues from Operations

Revenues for 2007 were Ps. \$12,190.6 million, compared to Ps. \$6,675.7 million in 2006, an increase of Ps. \$5,514.9 million or 83%. The number of access lines increased to 932,292 from 792,532, an increase of 18%, and our average revenue per user decreased from Ps. 590 pesos in 2006 to Ps. 673 pesos in 2007.

Local services. Local service revenues for the twelve-month period ended December 31, 2007, totaled Ps. 5,336.6 million, a growth of Ps. 1,006.6 million, or 23%, from Ps. 4,330.0 million recorded in 2006. This change is due to increased monthly rents, measured service and cellular revenues due to a higher number of lines in service.

Long distance services. In 2007, long distance service revenues increased to Ps. 1,532.2 million from Ps. 583.6 million registered in 2006, an increase of Ps. 948.6 million, or 163%, primarily due to the consolidation of Avantel not reflected in October and November 2006 and by the continued penetration of bundled commercial offers that incorporate long distance minutes. *Data & Network.* Data and network service revenues increased to Ps. 2,513.8 million for the twelve-month period ended December 31, 2007, compared to Ps. 459.1 million in 2006, an increase of Ps. 2,054.7 million, or 448%. The increase is explained by an increase in dedicated Internet and VPNs services provided primarily to business customers.

International traffic. Revenues generated from international calls terminated in Mexico totaled Ps. 1,210.2 million in 2007, compared to Ps. 552.8 million in 2006, an increase of Ps. 657.4 million, or 119%. This growth is due mainly to the consolidation of Avantel.

Other services. Revenue from other services accounted for Ps. 1,597.8 million in 2007, an increase of Ps. 847.6 million, or 113%, from Ps. 750.2 million registered in 2006, primarily due to an increase of Ps. 229.9 million from integrated services and Ps. 75.3 million from the sale of customer premises equipments ("CPEs"). Other revenues that includes activation fees, interconnections and special services among others made up the difference.

Cost of Revenues and Operating Expenses

Cost of Revenues. Cost of revenues was Ps. 4,504.7 million in 2007, compared to Ps. \$2,104.3 million in 2006, an increase of Ps. 2,400.4 million, or 114%, year-over-year. This growth was primarily due to Ps. 104.8, Ps. 1,168.2 and Ps. 53.3 million increases in costs related to the "calling party pays" scheme, long-distance termination costs and costs related to integrated services, respectively.

Operating Expenses. For the twelve-month period ended December 31, 2007, operating expenses increased to Ps. 3,601.4 million, from Ps. 2,260.1 million in 2006, an increase of Ps. 1,341.3 million, or 59%. Among others, increases of Ps. 734.6 million, Ps. 94.6 million and Ps. 53.3 million in personnel, consulting and outsourcing and advertising expenses, respectively explain this growth.

Depreciation and Amortization. Depreciation and amortization totaled Ps. 2,690.7 million in 2007, compared to Ps. 1,560.1 million in 2006, a growth of Ps. 1,130.6 million or 72%. The increase is due to the organic expansion in 2007 and the consolidation of Avantel not reflected in October and November 2006.

Year Ended December 31, 2006 Compared with Year Ended December 31, 2005

Revenues from Operations

Revenues from operations increased to Ps. 6,675.7 million for 2006 from Ps. 5,362.4 million for 2005, an increase of Ps. 1,313.3 million, or 24%. The number of access lines increased to 792,532 in 2006 from 605,904 in 2005, an increase of 31%, and our average revenue per user decreased from Ps. 672 pesos in 2005 to Ps. 590 pesos in 2006.

Local services. Local service revenues increased to Ps. 4,330.0 million for 2006 from Ps. 3,770.8 million for 2005, an increase of Ps. 559.2 million, or 15%. This change is due to increased monthly rents, value added services and cellular revenues due to a higher number of lines in service. *Long distance services.* Long distance services revenues increased to Ps. 583.6 million for 2006 from Ps. 487.9 million for 2005, an increase of Ps. 95.7 million, or 20%. This is a consequence of a higher number of access lines and a larger penetration of bundled offers including long distance minutes.

Data & Network. Data and network service revenues increased to Ps. 459.0 million for the twelve-month period ended December 31, 2006, compared to Ps. 215.6 million in 2005, an increase of Ps. 243.4 million, or 113%. This increase is explained by the contribution from Avantel in December and the remaining growth balance is due to increased data services provided primarily to business customers.

International traffic. Revenues generated from international calls terminated in Mexico totaled Ps. 552.8 million in 2006, compared to Ps. 509.3 million in 2005, an increase of Ps. 43.5 million, or 8.5%. This growth is due to handling more international traffic in 2006 compared to the previous year.

Other services. Revenue from other services increased to Ps. 750.2 million in 2006 from Ps. 378.7 million during 2005, an increase of Ps. 371.5 million, or 98.1%. The increase was due to Ps. 118.6 million contributed from integrated services and Ps. 82.4 million from the sale of customer premises equipments (“CPEs”). Activation fees and other revenues related to a higher number of lines in service made up the difference.

Cost of Revenues and Operating Expenses

Cost of Revenues. Cost of revenues from operations increased to Ps. 2,104.3 million for 2006 from Ps. 1,673.9 million in 2005, an increase of Ps. 430.3 million, or 26%. This growth was primarily due to Ps. 110.4 and Ps. 106.5 million increases in costs related to the “calling party pays” scheme and long-distance termination costs, respectively. Additionally, costs related to integrated services totaled Ps. 75.4 million, being these services not provided prior to the acquisition of Avantel.

Operating expenses. Operating expenses increased to Ps. 2,260.1 million for 2006 from Ps. 1,821.8 million for 2005, an increase of, Ps. 438.2 million or 24%. Increased personnel expenses of Ps. 208.5 million, expenses related to Avantel’s integration and other expenses related to the five new cities opened in 2006 were the main factors that generated this increase.

Depreciation and Amortization. Depreciation and amortization from continuing operations increased to Ps. 1,560.1 million for 2006 from Ps. 1,220.2 million for 2005, an increase of Ps. 339.8 million, or 28%. The year-over-year increase reflects our organic capital expenditures, and the acquisition of Avantel’s assets.

US GAAP Reconciliation

We describe below the principal differences between Mexican GAAP and US GAAP that relate to the operations of Axtel. See Note 25 to the audited consolidated financial statements for reconciliation to US GAAP of shareholders’ equity and net income (loss) for the respective periods presented.

Recognition of the effects of inflation on financial information. Under Mexican GAAP, the effects of inflation are reflected in financial statements. Such a convention has no counterpart under US GAAP. However, although Mexican GAAP includes the effects of inflation in financial statements, the SEC does not require the restatement of financial statements to reconcile the effects of the Mexican GAAP inflation accounting.

Preoperating expenses. Under Mexican GAAP, all expenses incurred while a company is in the preoperating or development stages are deferred and considered as a component of a company's assets. Such capitalized expenses are amortized on a straight-line basis for a period not exceeding 10 years after the corresponding asset commences operations. According to US GAAP, such preoperating or development expenses are expensed and reported as a deficit to shareholders' equity recorded during the developing stage.

Deferred income tax and employees statutory profit sharing. Under Mexican GAAP deferred income tax is accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Deferred income tax and employees statutory profit sharing is recognized only for timing differences arising from the reconciliation of book income to income for profit sharing purposes, on which it may reasonably be estimated that a future liability or benefit will arise and there is no indication that the liabilities or benefits will not materialize. Under US GAAP, deferred income tax and employees statutory profit sharing are determined under the asset and liability method recognizing the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss carryforwards.

Statement of changes in financial position. In accordance with Mexican GAAP, we present statements of changes in financial position in constant pesos. This presentation identifies the generation and application of resources representing differences between beginning and ending financial statements balances in constant pesos.

The changes in the consolidated financial statement balances included in our audited consolidated financial statements constitute cash flow activity stated in constant pesos (including monetary losses which are considered as cash losses in the financial statements presented in constant pesos). SFAS No. 95 does not provide guidance with respect to inflation adjusted financial statements. However, US GAAP requires that non-cash financing and investing transactions should be excluded from the statement of cash flows and reported in related disclosures.

Capitalization of interest. In accordance with Mexican GAAP, capitalization of interest or, during inflationary periods, comprehensive cost of financing or income incurred in the period of construction and installation of an asset is permitted. Under US GAAP, capitalization of interest is required for certain qualifying assets that require a period of time to get them ready for their intended use. The amount of interest to be capitalized is that portion of the interest cost incurred during the assets' acquisition period that theoretically could have been avoided if expenditures for the assets had not been made, and is not limited to indebtedness attributable to the asset.

Revenue recognition. In accordance with Mexican GAAP, we recognized activation fees received upon installation and activation of services when the customer has a contract with an indefinite term. Conversely, US GAAP SAB 104 indicates that the activation is deferred and recognized over the expected term of the customer relationship beginning on the date the service was installed.

Devaluation and Inflation

On December 20, 1994, the Mexican government responded to exchange rate pressures by increasing the upper limit of the then existing free market peso/US dollar exchange rate band by 15% and, two days later, by eliminating the band to allow the peso to fluctuate freely against the US dollar. This resulted in a major devaluation of the peso relative to the US dollar. While the noon buying rate had been Ps. 3.47 per US\$1.00 on December 19, 1994, by December 31, 1994 the noon buying rate had fallen to over Ps. 5.00 per US\$1.00, representing a 44.1%

devaluation. The peso continued to decline against the US dollar during 1995, closing at a noon buying rate of Ps. 7.74 per US\$1.00 on December 31, 1995, which represented a 54.8% devaluation relative to the US dollar for the year.

The Mexican economy began to recover in 1996 and 1997, as exchange rates stabilized, inflation decreased and real gross domestic product grew by 5.2% and 6.8%, respectively. However, the financial crisis in Asia and Russia, together with the weakness in the price of oil in 1998, which is a significant source of revenue for the Mexican government, contributed to renewed weakness in the peso, which devalued 22.7% relative to the US dollar. In 1999, the peso appreciated 4.0% relative to the US dollar. From 1999-2000, the peso-to-dollar denominated exchange rate remained relatively stable. In 2001, the peso-to-dollar exchange rate showed a slight recovery of 4.6% from Ps. 9.61 on December 31, 2000 to Ps. 9.17 on December 31, 2001. However, in 2002, the peso devalued 13.8% relative to the US dollar. In 2003, the peso devalued approximately 7.6% relative to the US dollar. During the years ended December 31, 2004, 2005 and 2006, the peso appreciated 0.8%, 4.6% and depreciated 1.6% (in nominal terms) respectively, relative to the US dollar. In 2007, the peso depreciated 1.1% (in nominal terms) respectively, relative to the US dollar.

Peso devaluation has contributed to sharp increases in inflation. Inflation, which had been 7.1% in 1994, increased to 52.0% and 27.7% in 1995 and 1996, respectively. After a reduction to 15.7% in 1997, inflation was 18.6% in 1998. In 1999, 2000 and 2001, the inflation rate decreased to 12.3%, 9.0% and 4.4%, respectively. In 2002, 2003, 2004 and 2005, the inflation rate was 5.7%, 4.0%, 5.2% and 3.3%, respectively. For the twelve month periods ending on December 31, 2006 and 2007, the inflation rates were 4.1% and 3.8%, respectively.

The general economic conditions in Mexico resulting from a devaluation of the peso and inflation may have a negative impact on Axtel's results of operations and financial condition, primarily as a result of:

- the resulting decrease in the purchasing power of Mexican consumers, which results in a decrease in the demand for telephony services;
- Axtel's inability, due to competitive pressures, to increase its prices in line with inflation; and
- an increase in the peso-carrying amount of its US dollar-denominated debt, reflecting the additional amounts of pesos required to meet such debt.

See Item 3.D. "Risk Factors—We may lose money because of peso devaluation."

Recent Accounting Pronouncements

Recently issued accounting pronouncements under Mexican GAAP

The CINIF has issued the following FRS, effective for years beginning after December 31, 2007, and which do not provide for earlier application.

- (a) **FRS B-10 "Effects of inflation"** - FRS B-10 supersedes Bulletin B-10 and its five amendments, as well as the related circulars and INIF (Interpretation of Financial Reporting Standards) 2. The principal considerations established by this FRS are: (i) the change in the value of the Investment Unit (UDI) may be used for determining the inflation for a given period; (ii) the election to use inventory replacement costs as well as specific indexation for fixed assets, is eliminated; (iii) an entity is only required to recognize the effects of inflation when operating in an inflationary economic environment (accumulated inflation equal to or higher than 26% in the most recent three-year period); and (iv) the accounts of Gain or Loss from Holding Non-monetary Assets (RETANM - Spanish abbreviation), Monetary Position Gains or Losses (REPOMO - Spanish abbreviation), and Deficit/Excess in Equity Restatement, will be reclassified to retained earnings, when the unrealized portion is not identified.

- (b) **FRS D-3 “Employee benefits”**- FRS supersedes Bulletin D-3, the portion applicable to Employee Statutory Profit Sharing (ESPS) of Bulletin D-4 and INIF (Interpretation of Financial Reporting Standards) 4. The principal considerations established by this FRS are: (i) a maximum of five years is established for amortizing unrecognized/unamortized items, and the option is provided for immediate recognition of actuarial gains or losses in results of operations; (ii) the recognition of an additional liability and related intangible asset and any related item as a separate element of stockholders’ equity, is eliminated; (iii) severance benefits are to be recognized directly in results of operations; and (iv) ESPS, including deferred ESPS, is to be presented in the statement of income as ordinary operations. Furthermore, FRS D-3 establishes that the asset and liability method required by FRS D-4 should be used for determining deferred ESPS, stating that any effects arising from the change are to be recognized in retained earnings, with no restatement of prior years’ financial statements.
- (c) **FRS D-4 “Tax on earnings”**- FRS supersedes Bulletin D-4 and Circulars 53 and 54. The principal considerations established by this FRS are: (i) the balance of the cumulative IT effects resulting from the initial adoption of Bulletin D-4 in 2000 is reclassified to retained earnings; (ii) AT is recognized as a tax credit (benefit), rather than as a tax prepayment; and (iii) the accounting treatment of ESPS incurred and deferred is transferred to FRS D-3, as mentioned in paragraph (b) above.
- (d) **FRS B-2 “Statement of cash flows”**- FRS supersedes Bulletin B-12 and paragraph 33 of Bulletin B-16. The principal considerations established by this FRS are: (i) the statement of cash flows replaces the statement of changes in financial position; (ii) cash inflows and cash outflows are reported in nominal currency units i.e. the effects of inflation are not included; (iii) two alternative preparation methods (direct and indirect) are established, without stating preference for either method. Furthermore, cash flows from operating activities are to be reported first, followed by cash flows from investing activities and lastly cash flows from financing activities; (iv) captions of principal items are to be reported gross; and (v) disclosure of the composition of those items considered cash equivalents is required.

Recently issued accounting pronouncements under US GAAP

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities – including an amendment of FASB Statement No. 115 (Statement 159). Statement 159 gives the Company the irrevocable option to carry most financial assets and liabilities at fair value that are not currently required to be measured at fair value. If the fair value option is elected, changes in fair value would be recorded in earnings at each subsequent reporting date. SFAS 159 is effective for the Company’s 2008 fiscal year. The Company is currently evaluating the impact the adoption of this statement could have on its financial condition, results of operations and cash flows.

In September 2006, the FASB issued SFAS No. 157, “Fair Value Measurements.” SFAS No. 157 clarifies the principle that fair value should be based on the assumptions that market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. Under SFAS No. 157, fair value measurements would be separately disclosed by level within the fair value hierarchy. In February 2008, the FASB approved FASB Staff Position FAS 157-2 (“FSP 157-2”) that permits companies to partially defer the effective date of SFAS No. 157 for one year for nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. FSP 157-2 did not permit companies to defer recognition and disclosure requirements for financial assets and financial liabilities or for nonfinancial assets and nonfinancial liabilities that are remeasured at least annually. SFAS No. 157 is effective for financial assets and financial liabilities and for nonfinancial assets and nonfinancial liabilities that are remeasured at least annually for the Company’s fiscal year beginning February 24, 2008. The Company will defer adoption of SFAS No. 157 for one year for nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. The Company is evaluating the effect the implementation of SFAS No. 157 will have on the consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), “Business Combinations” (“SFAS No. 141(R)”). SFAS No. 141(R) expands the definition of a business combination and requires the fair value of the purchase price of an acquisition, including the issuance of equity securities, to be determined on the acquisition date. SFAS No. 141(R) also requires that all assets, liabilities, contingent considerations and contingencies of an acquired business be recorded at fair value at the acquisition date. In addition, SFAS No. 141(R) requires that acquisition costs generally be expensed as incurred, restructuring costs generally be expensed in periods subsequent to the acquisition date and changes in accounting for deferred tax asset valuation allowances and acquired income tax uncertainties after the measurement period impact income tax expense. SFAS No. 141(R) is effective for the Company’s fiscal year beginning December 15, 2008 on a prospective basis for all business combinations for which the acquisition date is on or after the effective date of SFAS No. 141(R), with the exception of the accounting for adjustments to income tax-related amounts, which is applied to acquisitions that closed prior to the effective date of SFAS No. 141(R). The Company is evaluating the effect the implementation of SFAS No. 141(R) will have on the consolidated financial statements.

In December 2007, the FASB issued SFAS No. 160, “Noncontrolling Interests in Consolidated Financial Statements, an Amendment of ARB No. 51.” SFAS No. 160 changes the accounting and reporting for minority interests such that minority interests will be recharacterized as noncontrolling interests and will be required to be reported as a component of equity, and requires that purchases or sales of equity interests that do not result in a change in control be accounted for as equity transactions and, upon a loss of control, requires the interest sold, as well as any interest retained, to be recorded at fair value with any gain or loss recognized in earnings. SFAS No. 160 is effective for the Company’s fiscal year beginning December 15, 2008 with early adoption prohibited. The Company is evaluating the effect the implementation of SFAS No. 160 will have on the consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, “Disclosures about Derivative Instruments and Hedging Activities.” SFAS No. 161 amends and expands the disclosure requirements of SFAS No. 133 for derivative instruments and hedging activities. SFAS No. 161 is effective for the Company’s fiscal year beginning November 15, 2008 with early adoption permitted. SFAS No. 161 does not impact the consolidated financial statements and the Company is evaluating the effect the implementation will have on the Notes to Consolidated Financial Statements.

In September 2006, the FASB’s Emerging Issues Task Force reached a consensus on Issue No. 06-4, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements (EITF 06-4). EITF 06-4 provides guidance on the accounting for arrangements in which an employer owns and controls the insurance policy and has agreed to share a portion of the cash surrender value and/or death benefit with the employee. This guidance requires an employer to record a postretirement benefit, in accordance with FASB Statement No. 106, Employers’ Accounting for Postretirement Benefits Other Than Pensions” or APB Opinion No. 12, “Omnibus Opinion-1967, if there is an agreement by the employer to share a portion of the proceeds of a life insurance policy with the employee during the postretirement period. This guidance is effective for reporting periods beginning after December 15, 2007. The Company is in the process of assessing the impact of adopting EITF 06-4 on its results of operations and financial position; however, the company currently expects that additional liabilities may be required to be recognized upon implementation of the consensus based on the current terms of certain life insurance arrangements with executive officers of the Company.

Critical Accounting Policies

Our consolidated financial statements included elsewhere in this Form 20-F have been prepared in accordance with Mexican GAAP, which differ in significant respects from US GAAP. See Note 25 to our consolidated financial statements, included elsewhere in this Form 20-F, for a description and the effects of the principal differences between Mexican GAAP and US GAAP as they relate to us.

We have identified below the accounting policies we have applied under Mexican GAAP that are critical to understanding our overall financial reporting.

Income taxes, tax on assets, and employee's statutory profit sharing

Under Mexican GAAP, income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Significant judgment is required to appropriately assess the amounts of tax assets. Axtel records tax assets when it believes there will be enough future taxable income for the realization of such deductible temporary difference. If this determination cannot be made, a valuation allowance is established to reduce the carrying value of the asset.

Deferred income tax and employees statutory profit sharing is recognized only for timing differences arising from the reconciliation of book income to income for profit sharing purposes with respect to which it may reasonably be estimated that a future liability or benefit will arise and there is no indication that the liabilities or benefits will not materialize.

Recognition of the effects of inflation

Under Mexican GAAP, the financial statements are restated to reflect the loss of purchasing power (inflation) of their functional currency. The inflation effects arising from holding monetary assets and liabilities are reflected in the income statements as monetary position result. Inventories, property, systems and equipment and deferred charges, with the exception and the equity accounts, are restated to account for inflation using the Mexican National Consumer Price Index published by Banco de México (central bank). The result is reflected as an increase in the carrying value of each item. Income statement accounts are also restated for inflation into constant Mexican Pesos as of the reporting date.

Impairment of long-lived assets

The Company evaluates, at least once a year, the adjusted values of its property, systems and equipment and other non-current assets subject to amortization to determine whether there is an indication of potential impairment or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed off are separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated.

Revenue recognition

Our revenues are recognized when earned, as follows:

- *Local calling services.* We generate revenue by enabling our customers to originate and receive an unlimited number of calls within a defined local service area. Customers are charged a flat monthly fee for basic service, a per call fee for local calls ("measured service"), a per minute usage fee for calls completed on a cellular line ("calling party pays" or "CPP calls") and a monthly fee for value-added services when requested by the customer. The costs related to the termination of our customers' cellular in other carriers' networks are charged to cost in the same month that the revenue is earned.

- *Long distance services.* We generate revenues by providing long distance services for our customers' completed calls. The costs related to the termination of our customers' long distance calls in other carriers' networks are charged to cost in the same month that the revenue is earned.
- *Data & Network.* We generate revenues by providing Internet, data and network services, like virtual private networks and dedicated private lines. The costs related to providing Internet, data and network services to our customers are charged to cost in the same month that the revenue is earned.
- *International Traffic.* We generate revenues terminating international traffic from foreign carriers. The costs related to the termination of international traffic are charged to cost in the same month that the revenue is earned.
- *Other Services.* We generate revenues from other services, which include among others, activation fees, equipment installation and customer premises equipment ("CPE") for new customers as well as custom-made integrated telecommunications services to corporate customers.

Other costs and expenses related to sales and marketing, costs of leasing land related to our operations and maintenance of the network, billing, payment processing, operator services and our leasing of private circuit links are recorded as incurred.

On December 17, 2003, the SEC issued Staff Accounting Bulletin No. 104, "Revenue Recognition in Financial Statements" (SAB 104). This bulletin summarizes the point of view of the SEC in the recognition of revenues in the financial statements according to US GAAP. The SEC concluded that only when all the following conditions are met is revenue recognition appropriate:

- (a) there is persuasive evidence of an agreement;
- (b) the delivery was made or the services rendered;
- (c) the sales price to the purchaser is fixed or determinable;
- (d) collection is reasonably assured.

SAB 104, specifically in Topic 13A, Question 5, discusses the situation of recognizing as revenue certain non-refundable cash items. SAB 104 provides that the seller should not recognize non-refundable charges generated in certain transactions when there is continuous involvement by the vendor.

One of the examples provided by SAB 104 is activation revenues from telecommunication services. The SAB concludes that unless the charge for the activation service is an exchange for products delivered or services rendered that represent the culmination of a separate revenue-generating process, the deferral method of revenue is appropriate.

Based on the provisions and interpretations of SAB 104, for purposes of the US GAAP reconciliation, we have deferred the activation revenues over a three-year period starting in the month such charge is originated. This period was determined based on our experience. The net effect of the deferral and amortization is presented in the US GAAP reconciliation presented in this Form 20-F.

Estimated useful lives of plant, property and equipment

Axtel estimates the useful lives of particular classes of plant, property and equipment in order to determine the amount of depreciation expense to be recorded in each period. Depreciation expense is a significant element of its costs, amounting in 2007 to Ps. 2,299.6 million, or 21% of its operating costs and expenses.

The estimates are based on historical experience with similar assets, anticipated technological changes and other factors, taking into account the practices of other telecommunications companies. We review estimated useful lives each year to determine whether they should be changed, and at times we have changed them for particular classes of assets. We may shorten the estimated useful life of an asset class in response to technological changes, changes in the market or other developments.

Derivative financial instruments

The Company accounts for derivatives and hedging activities in accordance with Bulletin C-10 for Mexican GAAP and FASB Statement No. 133, for US GAAP, Accounting for Derivative Instruments and Certain Hedging Activities, as amended, which require that all derivative instruments be recorded on the balance sheet date at their respective fair values, including those derivatives embedded in financial or non financial contractual agreements.

The Company uses financial derivative instruments in order to manage financial exposures, especially foreign exchange related, and rates related. According to NIF C-10 and FASB-133, allows to account such operations as a hedging operation if it accomplishes certain requirements as effectiveness proves, and to avoid the recording of volatility in derivative instruments fair values in the income statement. The Company accounts the operations with financial derivative instruments with hedging activities into two main classifications: (i) Fair value hedging and (ii) Cash flows hedging.

In spite of last paragraph, the Company has accounted operations with financial derivative instruments under the classification of trade, which fair value have been accounted directly in the income statement. This is due to the fact that some operations did not accomplish some of the requirements in actual norms to be registered under accounting hedge model, even though these operations are hedging activities highly effective.

The Company has financial derivative instruments that are registered as fair value hedge and the accounting register is realized by taking the changes in the fair value and the changes in the fair value of the risk primary position to the results of the year, for their compensation. For the financial derivative instruments registered as cash flow hedging the Company registers in the comprehensive income the change in the fair value of them and at the moment when a profit or loss is realized, is registered at the results of the Company, recycling the comprehensive income.

The ineffectiveness portion of the change in the fair value of a derivative instrument that qualifies as a hedging activity is reported in the income statement.

The Company will discontinue hedge accounting prospectively when it is determined that the derivative is no longer effective in offsetting changes in the fair value or cash flows of the hedged item, the derivative expires or is sold, terminated, or exercised. In any of these cases the fair value of the financial instrument is recognized directly in the income statement

Inventory

We periodically examine our inventory in order to determine its obsolescence. Based on these examinations, we might be required to establish reserves to provide for obsolescence. To date, those circumstances have not arisen to establish such a reserve.

Doubtful Accounts

We believe that proper management of our working capital is essential to successful management of our finances generally. For this reason, controlling and monitoring of our accounts receivable is a priority in daily financial management. In furtherance of the above, we have established a policy of reserving for all balances over 30 days past due.

Business Combinations

To account for the acquisition of Avantel, the Company followed guidelines established in FRS B-7 “Business Combinations”, which was effective since January 1, 2005. The following procedures were followed by Axtel: a) the acquisition was accounted for by the purchase method of accounting; b) the cost of Avantel were allocated to the assets acquired and liabilities assumed based on their estimated fair value at the date of acquisition; c) an account for identifiable intangible acquired assets was created; and d) the negative goodwill was reduced proportionately from the fixed assets and intangibles acquired, net of taxes.

B. Liquidity and Capital Resources

Liquidity and Capital Resources

Historically we have relied primarily on vendor financing, the proceeds of the sale of securities, internal cash from operations and the proceeds from bank debt to fund our operations, capital expenditures and working capital requirements. Although we believe that we would be able to meet our debt service obligations and fund our operating requirements in the future with cash flow from operations, we may seek additional financing in the capital markets from time to time depending on market conditions and our financial requirements. We will continue to focus on investments in property, systems and equipment (fixed assets) and working capital management, including the collection of accounts receivable and management of accounts payable.

Net resources provided by operating activities was Ps. 3,226.7 million, Ps. 2,532.0 million and Ps. 1,524.1 million for the years ended December 31, 2007, 2006 and 2005, respectively.

Net resources used in investing activities was Ps. 2,556.4 million, Ps. 8,800.6 million and Ps. 1,825.8 million for the years ended December 31, 2007, 2006 and 2005, respectively. These cash flows primarily reflect investments in property, systems and equipment of Ps. 2,486.0 million, Ps. 7,854.5 million and Ps. 1,767.0 million for the years ended December 31, 2007, 2006 and 2005, respectively.

Net resources provided by (used in) financing activities from continuing operations was Ps. (318.6) million, Ps. 5,449.0 million and Ps. 1,725.0 million for the years ended December 31, 2007, 2006 and 2005, respectively.

Since our inception, we have invested over Ps. 21,968.6 million as we built out our infrastructure. We expect to make additional investments in future years as we selectively expand our network into other areas of Mexico in order to exploit market opportunities as well as to maintain our existing network and facilities.

Indebtedness

During the twelve-month period ended on December 31, 2006, we incurred in significant new indebtedness to finance the acquisition of Avantel. In addition, in February 2007, we prepaid Ps. 3,383.4 million (US\$311.0 million) of the Bridge Loan with the proceeds of the Senior Note we issue on February 1, 2007 due on 2017. See Item 11 “Quantitative and Qualitative Disclosures About Market Risk”, for hedging transactions related to our indebtedness. The following table summarizes our total debt, currency and interest rate structure as of December 31, 2007.

	Amount	Currency	Interest Rate
2012 Syndicated Term Loan - peso tranche	1,042.4	MXN	Floating rate
2012 Syndicated Term Loan - US dollar tranche	1,197.7	USD	Floating rate
2013 Senior Notes	1,765.8	USD	Fixed rate
2017 Senior Notes	2,988.2	USD	Fixed rate
Avantel - Telmex Capital Lease Obligation	534.3	MXN	Fixed rate
Other Leasings	120.5	MXN and USD	both

Notes Premium and Accrued Interest	108.1	n.a.	n.a.
Total Debt	7,757.0		

All financial contracts and indentures governing Company's indebtedness do not limit the ability of subsidiaries to transfer funds or pay dividends to the Company. The average life of Axtel's debt is 7 years approximately. The following table summarizes the maturity profile of the Company's indebtedness as of December 31, 2007:

Year	Million Ps.
2008	159.3
2009	175.0
2010	1,088.9
2011	1,023.7
2012	448.0
2013	1,765.8
2017	2,988.2
OTHERS:	
Notes Premium	27.3
Accrued Interest	111.8
Var. Fair Value Swaps	(31.0)
Total Debt as of Dec 31, 2007	7,757.0

The most relevant financial covenants on existing debt are the following:

2012 Syndicated Loan

- (i) Net Worth as of the end of any fiscal quarter not less than 80% of the Net Worth as of December 31, 2006,
- (ii) Consolidated EBITDA to interest ratio to be greater than 3.0x as of the end of any fiscal quarter, commencing with the fiscal quarter ending September 30, 2006,
- (iii) Consolidated Senior Indebtedness to EBITDA ratio not greater than 3.0x as of the end of any fiscal quarter, commencing with the fiscal quarter ending September 30, 2006.

2013 Senior Notes

- (i) Consolidated Indebtedness to EBITDA ratio not greater than 4.0x as of the end of any fiscal quarter.

2017 Senior Notes

- (i) Consolidated Indebtedness to EBITDA ratio not greater than 4.0x as of the end of any fiscal quarter.

As of December 31, 2007, the Company has no material capital expenditures commitments.

Capitalization of preoperating expenses

We commenced commercial operations in June 1999. As permitted under Mexican GAAP, during our preoperating stage we were able to capitalize all of our general and administrative expenses and our net comprehensive cost of financing.

Beginning in June 1999, we are required to amortize all previously capitalized general and administrative expenses and to depreciate all previously capitalized net comprehensive cost of financing. These capitalized preoperating expenses are amortized on a straight-line basis for a period not exceeding ten years.

C. Research and development, patents and licenses, etc.

Not applicable.

D. Trend information.

The following discussion contains forward-looking statements that reflect our current expectations and projections about future events based on our knowledge of present facts and circumstances and assumptions about future events. In this Form 20-F, the words "expects," "believes," "anticipates," "estimates," "intends," "plans," "probable" and variations of such words and similar expressions are intended to identify forward-looking statements. Such statements necessarily involve risks and uncertainties that could cause actual results to differ.

In 2007, we made significant progress in the integration of Avantel, consolidating our position as the largest fixed-services telecommunications company in Mexico measured by lines in service, revenues, and EBITDA, after the incumbent. Our robust network and comprehensive portfolio of products and services allowed us to continue growing in existing cities and commencing operations in 10 new cities in 2007. We expect to continue growing primarily from customer acquisitions in our current markets as we continue to expand our coverage and capacity in the major metropolitan areas that we currently serve. We also expect to expand into selected geographies we do not yet serve through organic growth and, possibly, strategic acquisitions or commercial agreements. The Mexican telecommunications industry is highly influenced by various factors, such as: (i) competition in local services, long distance, data, internet, voice over internet protocol, or VoIP, services and video; (ii) ability to attract subscribers; (iii) changes and developments in technology, including our ability to upgrade our networks to remain competitive and our ability to anticipate and react to frequent and significant technological changes; (iv) the effects of governmental regulation of the Mexican telecommunications industry; (v) declining rates for long distance traffic; and (vi) other factors described in this Form 20-F.

Therefore, a number of factors that have been particularly significant to the results of operations for the periods discussed in this Form 20-F, and the expected results for upcoming years, requires an appreciation of the telecommunications industry in Mexico, competition from existing and new entrants, prices in local and long-distance services, economic conditions in Mexico and the U.S.A., exchange and inflation rates, among many other factors described in this Form 20-F.

E. Off-balance sheet arrangements.

As of December 31, 2007, the Company maintains the following stand-by letters of credit and performance and surety bonds, that due to their contingency nature, are not reflected in our balance sheet.

Issuer	Type	US Dollars (in Thousands)	Pesos (in Thousands)
Avantel Infraestructura S. de R.L. de C.V	Quality	0.0	2,000.0
	Performance	109.7	0.0
	Performance	0.0	56,731.2
Avantel S. de R.L. de C.V.	Leasing	0.0	4,005.2

	Concession	0.0	2,828.3
	S-By L/C in favor of Telmex	60,000.0	0.0
	Performance	2.9	0.0
	Performance	0.0	64,805.7
Avantel, S.A. A. en P.	Performance	1.3	
	Performance		2,812.6
Avantel, S.A.	Performance	0.0	4,020.1
Axtel, S.A.B. de C.V.	Leasing	0.0	1,046.6
	Quality	0.0	1,746.3
	Concession	0.0	1,213.7
	Performance	0.0	26,186.3
Servicios Axtel S.A. de C.V.	Others	0.0	254.9
Instalaciones y Contrataciones S.A. de C.V.	Others	0.0	0.0
TOTAL		60,114.0	167,650.9

F. Tabular disclosure of contractual obligations.

The following table discloses aggregate information about our contractual obligations as of December 31, 2007, and the periods in which payments are due.

	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
		pro forma, payments due by period			
		(US\$ in millions)			
Debt maturing within one year	14.7	14.7	—	—	—
Long-term debt	689.1	—	115.4	136.2	437.5
Interest payments	360.9	55.3	107.7	85.6	112.3
Operating leases	130.1	23.3	36.3	24.6	45.9
Total contractual cash obligation	<u>1,194.8</u>	<u>93.3</u>	<u>259.4</u>	<u>246.4</u>	<u>595.7</u>

Item 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

A. Directors and Senior Management

Pursuant to our bylaws (*estatutos*) and Mexican law, management is entrusted to a Board of Directors and a Chief Executive Officer. The Board of Directors is composed of a maximum of 21 regular members and their respective alternate directors, as approved by a shareholders meeting. At least 25% of the members of the Board of Directors must be independent pursuant to the new Mexican Securities Market Law. Our Board of Directors currently is comprised of nine regular members and nine alternate directors. Pursuant to our bylaws and Mexican law, the members of the Board of Directors remain in office for thirty days after their resignation or conclusion of the term to which they were appointed unless replaced; the Board of Directors may appoint provisional members.

The following table presents information concerning our directors and executive officers as of April 25, 2008:

Officer	Position
Tomás Milmo Santos.....	Chairman, Director and Chief Executive Officer
Patricio Jiménez Barrera.....	Chief Financial Officer and Director

Officer	Position
Andres Velázquez Romero(1)	Executive Director - Mass and Business Markets and Alternate Director
Bruno Gustavo Ramos Maza	Executive Director - Strategic Accounts
Ivan Alonso Hernandez	Executive Director - Technology
Alberto de Villasante Herbert(1)	Executive Director - Negotiations, Alliances and Institutional Relations and Alternate Director
Jose Eloy Valerio Treviño	Vice President of Human Resources
Gerardo Gonzalez Villarreal	Audit Director
Federico Gil Chaveznavia	General Counsel
Thomas Milmo Zambrano	Director
Alberto Santos de Hoyos	Director
Lorenzo H. Zambrano Treviño	Director
Alberto Garza Santos	Director
Héctor Medina Aguiar	Director
Bernardo Guerra Treviño(2)(3)	Director
Fernando Quiroz Robles(2)(3)	Director
Lawrence H. Guffey(2)(3)	Director
Balbina Milmo Santos(1)	Alternate Director
Francisco Garza Zambrano(1)	Alternate Director
Alberto Santos Boesch(1)	Alternate Director
David Garza Santos(1)	Alternate Director
Ramiro Villarreal Morales(1)	Alternate Director
Mauricio Morales Sada(1)	Alternate Director
Javier Arrigunaga Gomez del Campo(1)	Alternate Director
Benjamin Jenkins(1)	Alternate Director

(1) The role of alternate director is to perform the role of the primary director if the primary director is not in attendance.

(2) Independent Directors.

(3) Member of audit and corporate practices committee.

Set forth below is a summary of the business experience, functions, areas of expertise and principal outside business interests of our current directors, alternate directors and senior management. The business address for each of our current directors, alternate directors and senior management is Blvd. Gustavo Diaz Ordaz km. 3.33 No. L-1, Col. Unidad San Pedro, San Pedro Garza García, N.L., Mexico, CP 66215.

Tomás Milmo Santos has held the position of Chief Executive Officer of Axtel since 1994 and Director since October 1997. Mr. Milmo was also appointed Chairman of the Board of Directors in October 2003. Prior to joining Axtel, Mr. Milmo worked at Carbonifera de San Patricio, S.A. de C.V., a medium sized mining company in Mexico. In 1988 he was named CEO of that same company, holding this post until 1990, when he founded and became CEO of Milmar, S.A. de C.V., a housing development company that developed and sold over 10,000 homes between 1990 and 1993. He is a member of the Board of Directors of Cemex, S.A. de C.V., HSBC Mexico S.A., ITESM (Tec de Monterrey) and Universidad de Monterrey. Mr. Milmo holds a degree in Business Economics from Stanford University.

Patricio Jiménez Barrera has held the position of Chief Financial Officer of Axtel since January 1998. Prior to joining Axtel, Mr. Jiménez held a variety of finance-related positions, including an investment banker while at Invermexico Casa de Bolsa, a corporate treasurer while at Grupo Cydsa, S.A. and an investment banker, international treasurer, financing and correspondent banker while at Banca Serfin, S.A. (Mexico's third largest bank). Immediately prior to joining Axtel, Mr. Jiménez was responsible for the International Division at Banca Serfin, S.A. He is a member of the board of Seguros Banorte Generali and Pensiones Banorte Generali. Mr. Jiménez is a CPA and holds a degree from the Instituto Tecnológico y de Estudios Superiores de Monterrey.

Andrés Velázquez Romero has held the position of Executive Director of Mass and Business Markets in Axtel since March 2007. Prior to his current position, Mr. Velázquez held various Senior Management positions in Axtel including Executive Director for Central Region and Treasurer and Administrative Director. Mr. Velázquez has been responsible for treasury, risk management, credit lines, funding structure and foreign exchange for a number of banking institutions. Prior to joining Axtel, he was the COO in charge of the Banca Serfin International Agency in New York. Mr. Velázquez holds a degree in Economics from the ITAM in Mexico City.

Ivan Alonso Hernández has held the position of Executive Director of Technology since May 2002. Prior to his present position, Mr. Alonso held the Information Technology and Business Process Director positions at Axtel. Mr. Alonso has over 17 years experience in information technology and telecommunications areas with various companies, including Copamex Services & Real Estate Division. He has also collaborated with financing institutions including Banco del Atlantico & Banpais, with responsibility for the telecommunications group of its Northeast Division. Mr. Alonso holds a B.S. degree in Electronics and Communications Engineering from the Instituto Tecnológico y de Estudios Superiores de Monterrey.

José Eloy Valerio Treviño has held the position of Human Resources Vice President of Axtel since June 2007. Prior to his present position, Mr. Valerio was Director for Planning of Human Resources & Human Development at Axtel. Mr. Valerio has 26 years of experience in Human Resources and Administration in which he has carried out directive and consultant positions at Telecommunications, Paper and Cellulose, Tourism, Steel-Mechanical, Automotive and Pharmaceutical Industry. He was President of the Human Resources Executives Association (ERAC) and has been an Advisor for Academic, Governmental and Non-Governmental Organizations. Mr. Valerio holds a degree in Administration and an M.B.A.

Gerardo Gonzalez Villarreal has held the position of Audit Director in Axtel since March 2000. Prior to his current position, Mr. González held the Comptroller Director position. Mr. González has over 20 years experience in the audit, tax and accounting field. Prior to joining Axtel, he collaborated with international accounting firms such as Coopers & Lybrand International and DFK International, as well as a member of the Mexican and International DFK Audit Committee, in his capacity as Chairman in the Mexican accounting firms. Mr. González holds a degree as CPA & BA from Universidad del Norte.

Thomas Milmo Zambrano has been a Director of Axtel since October 1997 and held the position of Chairman of the Board of Directors from October 1997 until 2003. Mr. Milmo Zambrano was founder and Chairman of Grupo Javier S.A. de C.V., one of the largest housing development companies in Mexico, and of Incasa, S.A. de C.V., one of the largest aggregate producers in Mexico. He was also Chairman and CEO of both Carbonifera de San Patricio S.A. de C.V. and Carbon Industrial, S.A. de C.V., medium-sized mining companies in Mexico. He was a Director of Cemex, S.A. de C.V. until 1996.

Alberto Santos de Hoyos has been a Director of Axtel since October 1997. Mr. Santos is a director of Banco de México (regional), Grupo Cydsa, S.A., Sigma Alimentos and Seguros Comercial America. He has been Senator and Representative of the Mexican Congress; President and Vice-President of the Cámara de la Industria de Transformación de Nuevo León; Vice-President of the Mexican Confederación de Cámaras Industriales (CONCAMIN); and President of the Comisión de Productos Básicos of CONCAMIN; President of the Cámara Nacional de la Industria Azucarera y Alcoholera. Mr. Santos has also been Chairman of the Board, CEO and director of Gamesa. Mr. Santos holds a degree in Business Administration from the Instituto Tecnológico y de Estudios Superiores de Monterrey.

Lorenzo Zambrano Treviño has been a Director of Axtel since October 1997. Mr. Zambrano is the Chairman of the Board and CEO of Cemex, S.A. de C.V. He is also the Chairman of the Boards of Directors of the Instituto Tecnológico y de Estudios Superiores de Monterrey and the Americas Society. He is a member of the Executive Committee of Grupo Financiero Banamex Accival, S.A. de C.V. and the Salomon Smith Barney International Advisory Board. In addition, he is a member of the Board of Directors of Coca Cola Femsa, S.A. de C.V. and Televisa, S.A. He is also a member of the Advisory Council to the Stanford Graduate School of Business, the Museo de Arte Contemporáneo and the U.S.-Mexico Commission for Educational and Cultural Exchange. Mr.

Zambrano holds a B.S. degree in Mechanical Engineering from the Tecnológico de Monterrey and an M.B.A. from Stanford University.

Alberto Garza Santos has been a Director of Axtel since October 2003. Mr. Garza is the founder and Chairman of the Board of Promotora del Viento, S.A de C.V., a company dedicated to wind power in Mexico. He is also founder and Chairman of the Board of Promotora Ambiental, S.A.B. de C.V. (PASA), a leading waste management company in Mexico. Mr. Garza has engineered PASA's growth through multiple acquisitions, local unit start-ups, municipal concessions and the development of world-class landfills, including Mexico's first five privately owned landfills. In 2002, he positioned PASA as PEMEX's waste services provider of choice, winning various large, multiyear contracts.

Héctor Medina Aguilar has been a Director of Axtel since October 2003. Mr. Medina is the Executive Vice-President of Planning and Finance of Cemex, S.A. de C.V. and responsible for worldwide strategic planning and finance. Before joining Cemex, Mr. Medina was a Senior Manager at Grupo Alfa S.A. de C.V. He is Chairman of the Board of Universidad Regiomontana, Board Member of Minera Autlan, Cementos Chihuahua, Nacional Monte de Piedad and Mexfrutas. Mr. Medina is also member of the Advisory Committee of the Monterrey Institute of Technology (Instituto Tecnológico y de Estudios Superiores de Monterrey). Mr. Medina is a graduate of the Instituto Tecnológico y de Estudios Superior de Monterrey with a degree in Chemical Engineering. He also holds an M.S.C. degree in Management from the University of Bradford Management Center in England and an M.S. degree from the Escuela de Organizacion Industrial in Spain.

Bernardo Guerra Treviño has been a Director of Axtel since April 2006. Chief Executive Officer, and founding member in 1995, of MG Capital, an independent asset management firm in Mexico. From 1986 to 1995, he held different positions in financial institutions in Monterrey. Mr. Guerra holds an Industrial Engineering degree from the Instituto Tecnológico y de Estudios Superiores de Monterrey (ITESM). He currently serves in the Board of Director of Promotora Ambiental S.A.B. de C.V.(PASA) and Banco Ahorro Famsa S.A.

Fernando Quiroz Robles has been a Director of Axtel since April 2007. Mr. Quiroz is Chairman of the Board of Acciones y Valores Banamex (Accival) and Head of Corporate and Investment Banking Latin America of Citigroup. He is also member of the Administration and Investment Banking and Planning Committees at Citigroup, and member of the Executive Committee and Head of Specialized Banking at Banamex. Prior to his current position, Mr. Quiroz held various Senior Management positions in Banamex and Citigroup, including consumer banking, international banking, strategic planning and economic research. Mr. Quiroz joined Banamex in 1979.

Lawrence H. Guffey has been a Director of Axtel since May 2000. Mr. Guffey is also a Senior Managing Director in the Private Equity group of Blackstone. Mr. Guffey has led Blackstone's efforts in virtually all media and communications-related investments and has day-to-day responsibility for management of Blackstone Communications Advisors. Since joining Blackstone in 1991, Mr. Guffey has been involved in the execution of Blackstone's investments in Axtel, Bresnan Communications, Centennial Communications Corp., Crowley Wireless (Salmon PCS), CommNet Cellular, CTI Holdings, Encoda Systems (a LiveWire Media company), iPCS, Iusacell, LiveWire, PaeTec, TWFanch-one, TWFanch-two, Universo Online and U.S. Radio. Before joining Blackstone, Mr. Guffey worked in the Acquisitions Group at Trammell Crow Ventures, the principal investment arm of Trammell Crow Company. He currently serves as a director of Centennial Communications, Encoda Systems, Orcom and FiberNet. Mr. Guffey holds a degree from Rice University.

Javier Arrigunaga Gomez del Campo has been an Alternate Director of Axtel since April 2007. Mr. Arrigunaga is General Counsel and Head of Institutional Development for Citigroup Latinamerica and Banamex. Prior to his current position, Mr. Arrigunaga was Mexico's Ambassador at OECD and held various Executive positions in *Banco de Mexico* (Mexico's Central Bank) including General Counsel and Secretary of the Board of Governors. Mr. Arrigunaga has been Director of Aeromexico, Mexicana and Scotiabank. Mr. Arrigunaga holds a Law degree from the Universidad Iberoamericana and a L.L.M. from Columbia University.

Benjamin Jenkins has been an Alternate Director of Axtel for Mr. Lawrence H. Guffey since October 2003. Mr. Jenkins is a Principal in the Private Equity group of Blackstone. Since joining Blackstone in 1999, Mr.

Jenkins has been involved in the execution of Blackstone's investment in Axtel and has evaluated numerous industrial and communications investments. Previously, Mr. Jenkins was an Associate at Saunders Karp & Megrue. Prior to that, Mr. Jenkins worked in the Mergers & Acquisitions Department at Morgan Stanley & Co. Mr. Jenkins holds a B.A. in Economics from Stanford University and an M.B.A. from Harvard Business School.

Francisco Javier Garza Zambrano has been an Alternate Director of Axtel for Mr. Lorenzo Zambrano Trevio since June 17, 2005. Mr. Garza holds the position of Regional Chairman for Cemex México, United States and Foreign Trade. He has been Chairman of Cemex México, Cemex Panama, Venezolana de Cementos (Vencemos, S.A.), Vice President of Trading Cemex, S.A. and Chairman in charge of Cemex, S.A. de C.V.'s operations in the United States. Mr. Garza holds a degree in Business Administration from the Instituto Tecnológico y de Estudios Superiores de Monterrey and an M.B.A. from Cornell University-Johnson Graduate School of Management.

Alberto Santos Boesch has been an Alternate Director of Axtel for Mr. Alberto Santos de Hoyos since June 17, 2005. Mr. Santos has held the position of Chief Executive Officer at Empresas Santos, S.A. since the year 2000. He is a shareholder and director of Grupo Tres Vidas Acapulco, S.A., Desarrollos Marinos del Caribe (Hotel Mandarin Oriental Rivera Maya) and Gimnasio Body-tek, S.A. Mr. Santos is also a member of Generacion 2000 and Grupo México Nuevo. He is currently the Chairman of the Board of Directors of Grupo Monde (Mundo de Adiverzas theme park). Mr. Santos holds a degree in International Studies from the Universidad de Monterrey as well as international studies from Cushing Academy.

David Garza Santos has been an Alternate Director of Axtel for Mr. Alberto Garza since November 2005. Mr. Garza is Chairman of the Board of Directors and Chief Executive Officer of Maquinaria Diesel, S.A de C.V., a company which distributes Caterpillar, Ingersoll Rand and other construction equipment in Mexico and is also Chairman of the Board of Directors of Comercial Essex, S.A. de C.V., which is the largest distributor of Exxon Mobil lubricants in Mexico. Mr. Garza is also a member of the Board of Directors of Desarrollos Delta, S.A. de C.V., a real estate developer for residential, offices and resorts in Mexico, a member of the Board of Directors of Promotora Ambiental, S.A. de C.V., a leading waste management company in Mexico and also a member of the Advisory Committee of the School of Business Administration of the Instituto Tecnológico y de Estudios Superiores de Monterrey. Mr. Garza holds a degree in Business Administration from the Instituto Tecnológico y de Estudios Superiores de Monterrey.

Federico Gil Chaveznava has been an Alternate Director of Axtel for Mr. Tomás Milmo Santos since November 11, 2005. Mr. Gil has held the position of General In-House Counsel of Axtel since the year 2000. Previously, Mr. Gil was an Associate at the law firm D&A Morales y Asociados, S.C. Prior to that, Mr. Gil worked as Legal Counsel for Grupo Internacional de Inversiones. He was a legal advisor for Nuevo Leon State Congress. Mr. Gil holds a Licenciatura en Derecho (J.D. equivalent) from the Universidad de Monterrey.

Mauricio Morales Sada has been an Alternate Director of Axtel for Mr. Bernardo Guerra Treviño since April 2006. Mr. Morales Sada is president, and founding member in 1995, of MG Capital, an independent asset management firm in Mexico. From 1984 to 1995, he held different positions in financial institutions in Monterrey. Mr. Morales holds a Mechanical Engineering degree from the Instituto Tecnológico y de Estudios Superiores de Monterrey (ITESM), and currently serves in the Advisory Committee for the Business Incubator of the same institute.

Ramiro G. Villarreal Morales has been an Alternate Director of Axtel for Mr. Héctor Medina Aguiar since April 2006. Mr. Villarreal is the General Counsel of Cemex S.A de C.V. since 1987. Mr. Villarreal is also Secretary of the Board of Directors of Cemex S.A. de C.V. since 1995. Prior to joining Cemex, he served as Assistant General Director of Grupo Financiero Banpais (now part of Banco Mercantil del Norte S.A.) from 1985 to 1987. Mr. Villarreal is a graduate of the Universidad Autonoma de Nuevo Leon with a degree in law and holds a Master of Science in Finance from the University of Wisconsin.

Thomas Milmo Zambrano is the father of Tomas and Balbina Milmo Santos and cousin of Lorenzo Zambrano. Alberto Santos de Hoyos is the uncle of Tomas Milmo Santos and of Alberto Garza Santos and the father of Alberto Santos Boesch.

B. Compensation

For the year ended December 31, 2007, the aggregate compensation, including benefits, we paid to our directors, alternate directors and executive officers for services in all capacities was approximately US\$4.4 million.

In 2007, we and our subsidiaries incurred no costs to provide pension, retirement or similar benefits to our respective officers and directors pursuant to retirement plans or pension plans.

C. Board Practices

See “Item 6A. Directors and Senior Management” above. None of the directors of Axtel have any type of arrangement with Axtel whereby such director would receive benefits upon termination of employment.

Audit and Corporate Practices Committee

Pursuant to the new Mexican Securities Market Law, the Board of Directors in its supervision activities, will be assisted by one or more committees. For corporate practice matters, a committee will: provide its opinion to the Board of Directors with respect items of its concern as set forth under the new Mexican Securities Market Law; request expert opinions when considered advisable; call for shareholders meetings; provide support to the Board of Directors on reports needed to be prepared; and all other actions provided for under the new Mexican Securities Market Law or set forth under the bylaws. For audit matters, the same committee will: provide its opinion to the Board of Directors with respect items of its concern as set forth under the new Mexican Securities Law; evaluate the audit firm’s performance; discuss the financial statements for the company and recommend their approval to the Board of Directors; report the Board with the status of the internal control and audit systems of the company; render the opinion with respect the accounting policies and criteria and financial information submitted by the Chief Executive Officer; assist the Board of Directors by preparing the necessary reports; request expert opinions when considered advisable; request the relevant officers reports related with financial information as may be deemed necessary; investigate possible failures to comply with the policies and guidelines related to the operations, internal control systems and audit; receive information submitted by shareholders, directors, officers, employees or any third party with respect the items set forth on the items described in the previous item; inform the Board of Directors of any important irregularity detected in connection with the corrective actions proposed; call for shareholders meetings; verify that the Chief Executive Officer complies with resolutions adopted at the shareholders and board of directors meetings.

Our audit and corporate practices committee consists of Bernardo Guerra Treviño, Lawrence H. Guffey and Bertrand F. Guillot and their respective alternates, Mauricio Morales Sada, Benjamin Jenkins and Patricio D’Apice. Our shareholders meeting appointed Mr. Bernardo Guerra Treviño as Chairman of such committee.

Compensation Committee

the shareholders’ meeting of the Company approved the elimination of the compensation committee. Most of the duties and responsibilities of our former compensation committee will be assumed by our Board of Directors and our Audit and Corporate Practice Committee.

D. Employees

For the years ended December 31, 2005, 2006 and 2007, we had 2,940, 5,656 and 6,872 employees, respectively. All of our employees, except for our executive officers and certain other managers, are members of 3 different labor unions. We believe we have good relationships with our employees and their respective unions.

E. Share Ownership

Information on the ownership of our Share Ownership is given under “Item 7. Major Shareholders and Related Party Transactions.”

Item 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

A. Major Shareholders

Mexican law limits foreign ownership of those companies, like ours, owning certain telecommunications concessions to 49% of the voting stock of such companies. According to our records, Nacional Financiera, S.N.C, Institución de Banca de Desarrollo, Dirección Fiduciaria, as trustee of the CPO Trust owns 98.9% of the total shares of the Company. However, we have information that the following individuals or corporations directly or indirectly control 5% or more of the CPOs as of the date of this 20-F Report:

Name	Mexican / Foreign ⁽¹⁾
Tomás Milmo Santos	Mexican
Thomas Milmo Zambrano	Mexican
Alberto Santos de Hoyos	Mexican
Credit Suisse and BBVA (thru 3-year forward agreement with Imprá Café S.A. de C.V.) ⁽²⁾	Foreign
Blackstone Capital Partners III Merchant Banking Fund, L.P.	Foreign
Telecomunicaciones Holding Mx, S. de R.L. de C.V. (afiliada de Citigroup, Inc.)	Foreign

(1) Foreign holders must hold their Series B shares beneficially through CPOs or American Depositary Shares and pursuant to the provisions of the CPOs and American Depositary Shares have limited voting rights.

(2) Information including 3-year forward agreement between Imprá Café S.A. de C.V and Credit Suisse and BBVA on March 31, 2008.

For a full description on voting rights, please see Item 10.B memorandum and articles of incorporation, “Shareholder Meetings and Voting Rights”.

B. Related Party Transactions

Merger Agreement

On August 26, 2005, we and our former shareholder Telinor entered into a Merger Agreement providing for the Merger of Telinor with and into Axtel. The Merger was effective on September 13, 2005, after which Telinor ceased to exist and Axtel survived with its current corporate name. As a result of the Merger and pursuant to the terms of the Merger Agreement, the equity holders of Telinor are now shareholders of Axtel. The Merger was duly approved by an extraordinary shareholders’ meeting of Axtel and by an extraordinary partners’ meeting of Telinor.

Resolution of Shareholdings Dispute

On August 26, 2005, we, Telinor, Blackstone Capital Partners III Merchant Banking Fund L.P., Blackstone Offshore Capital Partners III L.P. and Blackstone Family Investment Partnership III L.P. (collectively, “Blackstone”), LAIF X sprl and LAIF IV Ltd. entered into a settlement agreement (the “Settlement Agreement”) pursuant to which all issues in an arbitration and other previously disclosed judicial proceedings in the United States

and Mexico relating to the issuance and ownership of certain of our shares were resolved. As a consequence of the Settlement Agreement, our shareholders held an ordinary and extraordinary shareholders meeting on August 26, 2005 pursuant to which, among other matters: they acknowledged and ratified all current shareholdings in Axtel including the issuance and subscription of the previously issued shares which were the subject of dispute; they authorized a decrease in an immaterial amount in Telinor's and Blackstone's ownership of our shares and an increase in the same amount in LAIF X sprl's ownership share, the Merger of Telinor and Axtel and a number of ancillary matters. All of the proceedings between the parties to the Settlement Agreement with respect to the matters previously in dispute have been definitely resolved.

Employment Retention Plan

In 2002 Axtel implemented a retention plan with respect to key employees in its sales and operations areas. The retention plan consisted of granting loans (each loan supported by a signed promissory note from the recipient) ranging from US\$10,000 to US\$100,000 to its key employees. The loans are not interest bearing and are not payable until the employee's employment with Axtel terminates. The total amount outstanding under these loans is US\$347,757, which includes: US\$92,170 to Andres Velázquez Romero (regional executive director) made on July 04, 2002; and US\$73,736 to Ivan Alonso Hernandez (Chief Technology Officer) made on July 05, 2002. The balance is distributed among four other key employees. This Employment Retention Plan was terminated at the end of 2002.

Banamex and/or Citigroup Inc. Agreements

Term Loan Facility

On November 30, 2006 we entered into an unsecured credit agreement with Citibank, N.A. as the Administrative Agent and Banamex as the Peso Agent, which was subsequently amended and restated on February 23, 2007, with a peso tranche in the aggregate amount of Ps. 1,042,362,416.67 and a US dollar tranche in the aggregate amount of US\$110,225,133.28. The term loan facility will mature in February 2012, with partial principal repayments payable quarterly starting in February 2010. The facility was syndicated with thirteen Mexican and international financial institutions.

Banamex Master Services Agreement

On November 27, 2006, Axtel, Avantel and Banamex entered into a master services agreement in which it was agreed that all service agreements in effect between Avantel and Banamex as of the date of the acquisition would survive with substantially identical terms and Axtel would provide telecommunications services (including, local, long distance and other services) to Banamex and its affiliates located in Mexico. During the term of the agreement, Banamex has agreed to contract with us for all of its current and future telecommunications needs and we have agreed to grant Banamex a most favored customer benefit with respect to rates and services levels. The initial term of this agreement is for five years, with automatic renewal for similar periods of five years if at that time of renewal we are not in breach of our obligations.

Banamex Credit Agreement

On December 7, 2006, Avantel Concesionaria and Banamex entered into a credit agreement under which Avantel Concesionaria issued a standby letter of credit in favor of Telmex and Telnor for an amount of US\$60.0 million to secure payment of services rendered by Telmex and Telnor in connection with the interconnection agreement dated as of October 1, 2006 among Telmex, Telnor and Avantel Concesionaria.

TelHolding Agreement

On November 30, 2006, we entered into an agreement with Tel Holding whereby Tel Holding was granted the option to subscribe for a number of shares (in the form of CPOs) representing up to 10% of our outstanding shares. Pursuant to this subscription agreement, Tel Holding subscribed and paid 82,151,321 Series B shares in the

form of CPOs on January 04, 2007. According to the terms of this subscription agreement, Tel Holding agreed not to transfer any of the CPOs acquired pursuant to such subscription agreement for a period of 364 days following the date of the acquisition of such CPOs, except in certain circumstances. In addition, Tel Holding was granted the right to request us to assist and support them, at our expense, in preparing and issuing placement prospectus and in participating in investor meetings for the offer of the CPOs, provided that (i) three years have elapsed since the acquisition of the CPOs by Tel Holding and (ii) such offer is made in any securities exchange where the CPOs representing our shares are trading at the time.

Other Transactions

- In March and May 2000, we and Gemini, S.A. de C.V. (a company controlled by Alberto Garza Santos, one of our shareholders) entered into lease agreements for the lease of land and property on which our corporate offices and a switch are located. For the period beginning January 1, 2002 and through December 31, 2007, we paid Gemini approximately US\$12.1 million in rental payments under these leases.
- In August 2002, we and Neoris de México, S.A. de C.V. (a consulting firm indirectly controlled by an affiliate of Imprá Café, S.A. de C.V., one of our shareholders) entered into a professional services agreement for the provision of technical assistance to us with respect to a customer care platform. For the period beginning August 1, 2002 and through December 31, 2003, we paid Neoris approximately US\$0.2 million in fees for services. In 2007, we paid an aggregate amount of US\$0.2 million in service fees.
- In April 2002, we and Instalaciones y Desconexiones Especializadas, S.A. de C.V. (a company controlled by the son of Alberto Santos de Hoyos, one of our shareholders) entered into a services agreement for the provision of installation services with regard to customer premise equipment. For the period beginning April 1, 2002 and through December 31, 2007, we paid them approximately US\$3.0 million in fees for services.
- We and Operadora de Parques y Servicios, S.A. de C.V. (a company controlled by the son of Alberto Santos de Hoyos, one of our shareholders) entered into a service agreement dated February 16, 2005, for the marketing and advertising of Axtel inside a theme park. For the period beginning January 1, 2002 and through December 31, 2007, we paid them approximately US\$1.1 million in related fees.
- Fundación Axtel A.C., a non-profit charity, was founded in 2005 to promote provide assistance in the communities where we operate. Among others, Tomas Milmo Santos and Patricio Jimenez serve as Directors in Fundación Axtel. For the twelve-month period ended December 31, 2007, we contributed US\$1.6 million to Fundación Axtel.
- On November 24, 2006, our shareholders Thomas Milmo Zambrano, Maria Luisa Santos de Hoyos, Alberto Santos de Hoyos, Tomas Milmo Santos and Imprá Café, S.A. de C.V., entered into an shareholders agreement whereby they agreed, among other things, to vote their shares (in any meeting of shareholders whereby the members of the board are to be elected) in order to designate one director (and its alternate) to our board as proposed jointly by Citigroup Inc., its subsidiaries and Tel Holding and its assigns, so long as such entities collectively hold or beneficial own (directly or indirectly through CPOs) shares representing between 7% and 10% of our outstanding shares.

C. Interests of Experts and Counsel

Not applicable.

Item 8. FINANCIAL INFORMATION

A. Consolidated Statements and Other Financial Information

See “Item 18. Financial Statements.”

B. Significant Changes

Not applicable.

Item 9. THE OFFER AND LISTING

A. Offer and Listing Details

Not applicable.

B. Plan of Distribution

Not applicable.

C. Markets

Not applicable.

D. Selling Shareholders

Not applicable.

E. Dilution

Not applicable.

F. Expenses of the Issue

Not applicable.

Item 10. ADDITIONAL INFORMATION

A. Share Capital

Not applicable.

B. Memorandum and Articles of Association

Bylaws

Below is a brief summary of certain significant provisions of our bylaws and applicable Mexican law. This description does not purport to be complete and is qualified in its entirety by reference to our bylaws and the provisions of applicable Mexican law. For a description of the provisions of our bylaws relating to the board of directors and audit and corporate practices committee, See “Item 6. Directors, Senior Management and Employees.”

Organization and Register

We are a *sociedad anónima bursátil de capital variable* organized under the laws of Mexico. We were incorporated in 1994 under the name Telefonía Inalámbrica del Norte, S.A. de C.V. Thereafter, on March 1999, our corporate name changed to Axtel, S.A. de C.V. Later, on December 2006, our corporate name changed to Axtel, S.A.B. de C.V.

Our corporate domicile is San Pedro Garza García, Nuevo León, Mexico, and our headquarters are located at Blvd. Gustavo Díaz Ordaz Km. 3.33, Colonia Unidad San Pedro, 66215, San Pedro Garza García, Nuevo León.

Our corporate purpose is to install, operate and exploit a public telecommunications network for the provision of telephony, internet and other value added telecommunication services to the public, using primarily fixed wireless technology, and/or use, utilize and exploit frequency bands of the radioelectric spectrum.

Board of Directors

Pursuant to our bylaws (estatutos) and Mexican law, management is entrusted to a Board of Directors and a Chief Executive Officer. According to Mexican law and our bylaws, our Board of Directors shall be composed of a maximum of 21 regular members and their respective alternate directors, as approved by a shareholders meeting. At least 25% of the members of the Board of Directors must be independent pursuant to the new Mexican Securities Market Law. Our Board of Directors currently is comprised of ten regular members and ten alternate directors. Pursuant to our bylaws and Mexican law, the members of the Board of Directors remain in office for thirty days after their resignation or conclusion of the term to which they were appointed unless replaced; the Board of Directors may appoint provisional members.

Capital Stock

Outstanding Capital Stock

Our capital stock consist of two series of shares of common stock without par value: Series A shares and Series B shares. Pursuant to Article 54 of the Mexican Securities Market Law and subject to the prior authorization of the CNBV, we may issue shares of a different series without voting rights, or with restricted voting rights, or with additional limitations of other corporate rights. The Shareholders' meeting approving such issuance shall determine the rights corresponding to the new series of shares issued.

Since we are a variable capital corporation, our capital stock must have a fixed portion and may have a variable portion. As of the date of this form, our outstanding capital consists of 8,769,353,223 shares representing only fixed capital. Neither our subsidiaries nor we may own our shares although there are limited instances in which we can repurchase our shares. See “—Share Repurchases” below.

Changes in Our Capital Stock, Preemptive Rights and Redemption

Our fixed capital stock may be increased or decreased by a resolution passed at a general extraordinary shareholders' meeting. The variable portion of the capital stock may be increased or decreased by a resolution passed at a general ordinary shareholders' meeting. Increases or decreases in the fixed or variable portion of the capital stock must be recorded in our registry of capital variations. Pursuant to Mexican law, our bylaws provide that changes in the variable portion of our capital stock do not require an amendment to the bylaws nor registration in the Public Registry of Property and Commerce to effect such changes. New shares cannot be issued unless the outstanding shares have been paid in full.

In the event of an increase in our capital stock (whether fixed or variable), the shareholders have preemptive rights to subscribe the newly issued shares in proportion to their holdings, except in the case of:

- shares issued in connection with capitalization of subscription premiums, retained earnings and other capital reserves and accounts in favor of all shareholders in proportion to their shareholdings;
- shares issued for placement in public offerings, if an extraordinary shareholders' meeting called for such purpose approves the issuance of shares and other requirements specified in Article 53 of the Mexican Securities Market Law are satisfied, including obtaining the prior written approval of the CNBV;
- shares issued in connection with mergers;
- shares issued as treasury shares in connection with the issuance of securities convertible into our shares in accordance with Article 210 *bis* of the Law of Negotiable Instruments and Credit Transactions (*Ley General de Títulos y Operaciones de Crédito*); and
- the resale of shares held in the treasury as a result of repurchases of shares conducted on the Mexican Stock Exchange.

The subscription period for the exercise of preemptive rights will be determined at the shareholders' meeting which approves the respective capital increase, provided that such period will not be less than 15 calendar days following the publication in the official gazette of our corporate domicile and in a newspaper of general circulation in our corporate domicile. Under Mexican law, preemptive rights cannot be waived in advance or assigned, or be represented by an instrument that can be negotiable separately from the corresponding share certificate.

Shares representing our capital stock are subject to redemption in connection with either (i) a reduction of capital stock or (ii) a redemption with retained earnings, which in either case must be approved by our shareholders. In connection with a capital reduction, the redemption of shares shall be made *pro rata* among the shareholders, or, if affecting the variable portion of the capital stock, as otherwise determined in the relevant shareholders' meeting; but, in no case shall the redemption price be less than the book value of such shares as determined pursuant to our latest balance sheet approved at a general ordinary shareholders' meeting. In the case of a redemption with retained earnings, such redemption shall be conducted (a) by means of a tender offer conducted on the Mexican Stock Exchange, in accordance with the Mexican Companies Law, the Mexican Securities Market Law and our bylaws, or (b) *pro rata* among the shareholders.

Variable Capital

According to the Mexican Securities Market Law and our bylaws, our shareholders holding shares of the variable portion are not entitled to the redemption right referred to in Article 220 of the Mexican Companies Law.

Share Repurchases

Pursuant to the Mexican Securities Market Law, our bylaws provide that we may repurchase our shares on the Mexican Stock Exchange at the prevailing market price. Share repurchases must be charged to either our net worth, if the repurchased shares remain in our possession, or to our capital stock, if the repurchased shares are converted into treasury shares. The general ordinary shareholders' meeting must approve, for each year, the aggregate amount allocated to share repurchases, which amount cannot exceed the total amount of our net profits, including retained earnings. Our Board of Directors must appoint an individual or group of individuals responsible for effecting share repurchases, and sales of repurchased shares. Repurchased shares cannot be represented at any shareholders' meeting. Share repurchases must be carried out, reported, and disclosed in the manner established by the CNBV.

Cancellation of Registration in the RNV

In the event that we decide to cancel the registration of our shares in the RNV or if the CNBV orders such cancellation, we and our shareholders who are deemed to have “control” of us will be required to, prior to such cancellation, make a tender public offer to purchase the shares, in accordance with Article 108 of the Mexican Securities Market Law. The offer price shall be at least the higher of (i) the average of the trading price on the Mexican Stock Exchange during the last 30 days on which the shares were quoted prior to the date on which the tender offer is made, during a period no longer than six months or (ii) the book value of such shares as determined pursuant to our latest quarterly financial information filed with the CNBV and the Mexican Stock Exchange. We and our shareholders who are deemed to have “control” shall form a trust and contribute to it, for a minimum period of six months, the amount needed to purchase, at the same price offered in the tender offer, all of the shares that were not tendered in the offer. Such trust must be maintained for at least six months. We and our shareholders who are deemed to have “control” are not required to make such public offer if the cancellation of the listing is approved by at least 95% of our shareholders and the aggregate amount of the shares to be tendered from the general public is less than 300,000 *Unidades de Inversión*, or UDIs. Pursuant to CNBV rules, shareholders deemed to have “control” are those that own a majority of our shares, have the ability to impose decisions at our shareholders’ meetings or have the ability to appoint a majority of the members of our Board of Directors.

Registration and Transfer

Our shares are represented by share certificates in registered form. Our shareholders may either hold their shares directly, in the form of physical certificates, or indirectly, in book-entry form through brokers, banks, other financial entities or other entities approved by the CNBV that have accounts with Indeval (“Indeval Participants”). Indeval will issue certificates registered in the name of any shareholder who may request them. We maintain a stock registry and only those persons listed in such stock registry, and those holding certificates issued in their name as registered holders directly or through any relevant Indeval Participants, will be recognized as shareholders by us. The transfer of shares must be registered in our stock registry. Transfers of shares deposited with Indeval shall be registered in book-entry form pursuant to the Mexican Securities Market Law.

Pursuant to the concessions, in the event that in one or a series of transactions, the subscription for or transfer of shares that represent ten percent (10%) or more of the capital stock of the Company is proposed:

- (i) We must give notice to the Ministry of Communication and Transportation (*Secretaria de Comunicaciones y Transportes* or “SCT”) of Mexico of the intention of the interested party to carry out the subscription or transfer, which notice shall include information about the interested party acquiring the shares;
- (ii) The SCT will have 90 days, from the date the notice is given, to object in writing, on reasonable cause, to the transaction; and
- (iii) If the transaction has not been objected by the SCT during the 90 day period, such transaction will be deemed as approved.

The transactions not objected to by the SCT may be recorded on our stock registry, any other authorizations required pursuant to applicable provisions must be obtained from the other authorities. The notice required by this paragraph will not be necessary if the subscription or transfer relates to shares that represent neutral investment under the terms of the Foreign Investment Law or to capital increases subscribed for by the existing shareholders, *provided* the participation proportion of each remains the same in the capital stock. If the party subscribing for or acquiring the shares is an entity, the notice referred to in this paragraph shall include all necessary information for the SCT to know the identity of any individual that has more than a ten percent economic interest in the capital stock of such entity.

In accordance with the CPO Trust, the transfer of CPOs or ADSs held by non-Mexican investors whose underlying shares represent 10% or more of our voting shares will not require the prior approval of the SCT provided the CPOs continue to qualify as “neutral investment” for purposes of Mexican law.

Shareholder Meetings and Voting Rights

General shareholders’ meetings may be ordinary or extraordinary. At every general shareholders’ meeting, each holder of shares is entitled to cast one vote per share.

General extraordinary shareholders’ meetings are those called to consider:

- extension of our duration or voluntary dissolution;
- an increase or decrease in the fixed portion of our capital;
- change of our corporate purpose or nationality;
- any merger or transformation into another type of company;
- issuance of preferred stock or bonds;
- any amendments to our bylaws;
- our spin-off;
- the redemption of shares with retained earnings;
- the cancellation of the registration of shares at the RNV or any stock exchange (except for automated quotation system).

General ordinary shareholders’ meetings are those called to discuss any issues not reserved to extraordinary meetings. General ordinary shareholders’ meeting must be held at least once each year, during the first four months after the end of each fiscal year, to:

- consider the annual reports of the Chief Executive Officer, the annual report of Board of Directors, and the annual report of the Audit and Corporate Practices Committee;
- discuss the allocation of profits for the preceding year;
- appoint the members of the Board of Directors and to determine their compensation, and to appoint the chairperson to the Audit and Corporate Practices Committee; and
- determine the maximum amount of resources allocated to share repurchases.

In order to attend a general shareholders’ meeting, holders of shares must be registered in our stock registry, or submit appropriate evidence of the title to their shares. Holders of shares do not have cumulative voting rights.

The quorum for the ordinary shareholders’ meeting is at least 50% of the outstanding shares, and resolutions may be taken by a majority of the outstanding capital stock. If a quorum is not met, a subsequent meeting may be called at which resolutions may be taken by the majority of the shares present, regardless of the percentage of outstanding shares represented at such meeting. The quorum for extraordinary shareholders’ meetings is at least 75% of the outstanding shares, but if a quorum is not present a subsequent meeting may be called. The

quorum for such subsequent meeting is at least 50% of the outstanding shares. Resolutions at an extraordinary general shareholders' meeting must be taken by the vote of at least 50% of the outstanding shares (including any taken at an extraordinary shareholders' meeting called following the adjournment of a prior meeting for lack of quorum).

Shareholders' meetings may be called by:

- the Board of Directors or the Audit and Corporate Practices Committee or their respective chairman;
- the shareholder representing at least 10% of the outstanding shares upon request to the chairman of the Board of Directors or of the Audit and Corporate Practices Committee to have such a meeting;
- A Mexican court in the event the Board of Directors or the Audit and Corporate Practices Committee does not comply with a valid request of the shareholders as described in the immediately preceding bullet point; and
- the Board of Directors or a Mexican court, at any shareholder's request, provided that no ordinary meeting has been held for two consecutive years to deal with the appointment of directors and the annual reports of the Chief Executive Officer, the Board of Directors and the Audit and Corporate Practices Committee .

Notices for meetings must be published in the official gazette of our corporate domicile or in a newspaper of general circulation in our corporate domicile with 15 days and 7 days notice, respectively for the first and second calls of general ordinary, extraordinary or special shareholders' meetings. Notices for meetings must contain the meeting's agenda and must be signed by the person or entity who called the meeting. In order to be admitted to a shareholders' meeting, the shareholders must be registered in our stock registry book and request the corresponding admittance letter to the meeting from the secretary of the Board of Directors. In exchange for the admittance letter, the shareholders must deposit their share certificates at our offices or present a receipt from any Indeval Participant indicating ownership by such person. A shareholder may be represented by an attorney-in-fact with a proxy letter issued in a special format according to Article 49 of the Mexican Securities Market Law.

Minutes of shareholders' meetings shall be signed by the president, the appointed examiners and the secretary of the meeting, and shall be recorded in the relevant minute book or, in the event that such recording is not possible, the minutes of shareholders' meeting must be formalized before a notary public. In any case, extraordinary meeting resolutions must always be formalized before a notary public and registered at the Public Registry of Commerce of Monterrey, Nuevo León.

Dividend and Liquidation Rights

Prior to any distribution of dividends, 5% of our net earnings must be allocated to a legal reserve fund, until such fund is equal to at least 20% of our paid-in capital stock. Additional amounts may be allocated to other reserve funds as the shareholders may determine, including the amount allocated by the shareholders' meeting for the repurchase of shares. The remaining balance, if any, may be distributed as dividends. Cash dividends on shares not held through Indeval will be paid against delivery of the respective dividend coupon, if any.

To the extent that we declare and pay dividends on our Shares, dividends will be payable in Pesos. The Depositary will convert Pesos received with respect to Series B shares underlying CPOs deposited with it into U.S. Dollars and distribute U.S. dollars to ADS holders, after deduction or upon payment of applicable fees and expenses, of the Depositary. Currently, there is no Mexican withholding tax or other Mexican tax levied on holders of Shares purchased outside Mexico on dividends paid in respect of such Shares. See "Taxation—Mexican Taxation."

Upon our dissolution, one or more liquidators must be appointed by an extraordinary general shareholders' meeting to wind up our affairs. All fully paid and outstanding shares will be entitled to participate equally in any distribution upon liquidation.

Purchase of Shares by Our Subsidiaries

Any company or entity of which we are the owner of the majority of its equity interest may not purchase, directly or indirectly, our Shares or shares of companies holding the majority of our Shares.

Antitakeover Protections

General. Our by-laws provide that, subject to certain exceptions, (i) any person that individually or together with one or more related persons wishes to acquire shares or beneficial ownership of shares, directly or indirectly, in one or more transactions, without limitation as to time, resulting in such person holding, individually and/or together with such other related persons, shares representing 15% or more of the outstanding Series A or Series B shares, as the case may be, must obtain the prior written approval of our Board of Directors and/or, at the discretion of the Board of Directors, our shareholders meeting, as the case may be; (ii) any person that individually or together with one or more related persons holds 15% or more of the outstanding Series A or Series B shares and wishes to acquire shares or beneficial ownership of shares, directly or indirectly, in one or more transactions, without limitation as to time, resulting in such person, individually or together with other related persons, holding 25% or more of the outstanding Series A or Series B shares as the case may be, must obtain the prior written approval of our Board of Directors and/or, at the discretion of the Board of Directors, our shareholders meeting, as the case may be; (iii) any person that individually or together with one or more related persons holds 25% or more of the outstanding Series A or Series B shares and wishes to acquire shares or beneficial ownership of shares, directly or indirectly, in one or more transactions, without limitation as to time, resulting in such person, individually or together with other persons, holding 35% or more of the outstanding Series A or Series B shares as the case may be, must obtain the prior written approval of our Board of Directors and/or, at the discretion of the Board of Directors, our shareholders meeting, as the case may be; (iv) any person that individually or together with one or more related persons holds 35% or more of the outstanding Series A or Series B shares and wishes to acquire shares or beneficial ownership of shares, directly or indirectly, in one or more transactions, without limitation as to time, resulting in such person, individually or together with other persons, holding 45% or more of the outstanding Series A or Series B shares as the case may be, must obtain the prior written approval of our Board of Directors and/or, at the discretion of the Board of Directors, our shareholders meeting, as the case may be; and (v) any person that is our competitor or a competitor of any of our subsidiaries that individually or together with one or more related persons wishes to acquire shares or beneficial ownership of shares, directly or indirectly, in one or more transactions, without limitation as to time, resulting in such person, individually or together with other related persons holding 5% or more of the outstanding Series A or Series B shares as the case may be, must obtain the prior written approval of our Board of Directors and/or, at the discretion of the Board of Directors, our shareholders' meeting, as the case may be.

Any person that acquires shares in violation of our antitakeover provision will not be recognized as owner or beneficial owner of such shares under our bylaws and will not be registered in our stock registry book. As a result, the violating shareholder will not be able to vote such shares or receive any dividends, distributions or other rights in respect of these shares. For purposes of this provision, pursuant to our bylaws the term "shares" includes instruments or securities that represent our shares, including CPOs and ADSs, and the term "competitor" means any person engaged, directly or indirectly, (i) in the business of fixed or wireless telephony in any form and/or (ii) in any activity in which we or any of our subsidiaries are engaged that represents 5% or more of our or our subsidiaries' consolidated income. The Board of Directors may authorize exceptions to the definition of "competitor."

Board of Directors and Shareholders Meetings Requirements and Approvals. To obtain the prior approval of our Board, a potential acquirer must properly deliver a written authorization request containing certain specific information regarding the proposed transaction. During the authorization process, certain terms will have to be complied with. Our Board of Directors may, without liability, refer the acquisition for the approval to our shareholders meeting. The determination of the Board of Directors to refer the decision to our shareholders meeting will be based on different factors such as potential conflicts of interest, fairness of the proposed price or the inability of the Board of Directors to meet having been called more than two times, among others. The Board of Directors may revoke any authorization previously granted prior to the date on which the transaction takes place if an offer which is better for our shareholders is received.

Mandatory Tender Offers in the Case of Certain Acquisitions. If either our Board of Directors or our shareholders at a general extraordinary shareholders' meeting, as the case may be, authorize an acquisition of our shares which results in an acquisition of at least 20% but not more than 40% of our capital stock, notwithstanding such authorization, then the acquiror must effect the acquisition by way of a cash tender offer for a specified number of shares equal to the amount authorized plus additional shares equal to 10% of the company's capital stock, to the extent that such acquisition does not exceed 50% of the common voting shares or triggers a change of control. In the event that our Board of Directors or our shareholders at a general extraordinary shareholders' meeting, as the case may be, approve an acquisition that would result in a change of control, the acquiror must effect the acquisition by way of a cash tender offer for 100% minus one share of our total outstanding capital stock at a price which cannot be lower than the highest of the following: (i) the book value of the shares as reported on the last quarterly income statement approved by the Board of Directors; or (ii) the highest closing price of the shares, on any stock exchange during any of the three hundred sixty-five (365) days preceding the date of the Board of Directors' resolution approving the acquisition; or (iii) the highest price paid for any shares, at any time, by the acquiror that individually or collectively, directly or indirectly, acquires the shares approved by the Board of Directors. Any tender offer to be conducted in accordance with the above will be subject to certain specific requirements. All holders of our shares must be paid the same price for their shares at a tender offer. The provisions of our bylaws summarized above regarding mandatory tender offers in the case of certain acquisitions are generally more stringent than those provided for under the Mexican Securities Market Law. Some of our by-laws provisions regarding mandatory tender offers in the case of certain acquisitions may differ from the requirements set forth in the Securities Market Law, provided that those provisions are more protective to minority shareholders than those afforded by law. In these cases, the relevant by-laws provisions, and not the relevant provisions of the Securities Market Law, will apply to certain acquisitions specified therein.

Exceptions. The provisions of our bylaws summarized above will not apply to certain specific acquisitions, such as those resulting from inheritance, those conducted by the person or persons controlling us, and those conducted by us, our subsidiaries or affiliates or any trust created by us or any of our subsidiaries, among others.

Amendments to the Antitakeover Provisions. Any amendments to these antitakeover provisions must be authorized by the CNBV and registered before the Public Registry of Commerce at our corporate domicile.

Other Provisions

Duration

Our corporate life under our bylaws is indefinite.

Appraisal Rights and Other Minority Protections

If and when our shareholders approve any change of our corporate purpose, jurisdiction of incorporation or corporate form, any shareholder who has voted against such change has the right to withdraw and receive the book value of his or her shares (as set forth in the latest balance sheet approved by the shareholders), if the request is made during the 15-day period following the adjournment of the meeting at which such action was approved.

Pursuant to the Mexican Securities Market Law, we are subject to a number of minority protections. These minority protections include provisions that permit:

- holders of at least 10% of our outstanding share capital to convene a shareholders' meeting in which they are entitled to vote;
- holders of at least 5% of our outstanding share capital to bring an action for civil liabilities against our directors, subject to certain requirements under Mexican law;

- holders of at least 10% of our Shares who are entitled to vote and are represented at a shareholders' meeting to request that resolutions with respect to any matter on which they were not sufficiently informed be postponed; and
- holders of at least 20% of our outstanding share capital to contest and suspend any shareholder resolution, subject to certain requirements under Mexican law.

In addition pursuant to the Mexican Securities Market Law we are also subject to certain corporate governance requirements, including the requirement to maintain an audit committee and to elect independent directors.

The protections afforded to minority shareholders and the fiduciary duties of officers and directors under Mexican law are generally different from, and not as comprehensive as, those in the United States and many other jurisdictions. The Mexican legal regime concerning director fiduciary duties has not been extensively interpreted by Mexican courts, unlike many states in the United States where duties of care and loyalty established by court decisions have helped to shape the rights of minority shareholders. Mexican civil procedure does not contemplate class action lawsuits or shareholder derivative actions, which allow shareholders in the United States to bring actions on behalf of other shareholders or to enforce rights of the corporation itself. Shareholders in Mexico cannot challenge corporate actions taken at shareholders' meetings unless they meet stringent procedural requirements. As a result of these factors, it is generally more difficult for our minority shareholders to enforce rights against us or our directors or principal shareholders than it is for shareholders of a U.S. company.

Actions Against Directors, Statutory Auditors and Members of Our Audit Committee

Actions against any director, statutory auditor or member of our audit and corporate practices committee may be initiated by resolutions passed at an ordinary shareholders' meeting. In the event our shareholders decide to initiate such action, the respective person immediately ceases to be in office. Additionally, shareholders representing not less than 5% of our outstanding shares may directly bring a civil liability action against any director or member of our audit and corporate practices committee, in accordance with Article 38 of the Mexican Securities Market Law. Any recovered damages with respect to the action will be for our benefit and not directly for the benefit of the shareholders bringing the action. There are no shareholders' class actions available under Mexican law.

Conflicts of Interest

A shareholder that votes on a business transaction having a conflict of interest may be liable for losses and damages to us, but only if the action could not have been approved without such shareholder's vote. Additionally, a member of the Board of Directors or a member of our audit and corporate practices committee having a conflict of interest must disclose such conflict and abstain from any deliberation or vote in connection therewith. A breach by any member of the Board of Directors or member of our audit and corporate practices committee to such obligations may result in such director being liable for damages and losses.

Suspension of Shareholders' Action

Holders of 20% of our outstanding shares may oppose any resolution adopted by a shareholders' meeting and file a petition for a court order for the temporary suspension of said resolution, within 15 days after the adjournment of the meeting at which the action was taken, if the challenged resolution violates Mexican law or our bylaws and opposing shareholders neither attended the meeting nor voted against the challenged resolution.

Foreign Investment Regulations

Foreign investment in the capital stock of Mexican companies is regulated by the Foreign Investment Law and the regulations thereto, or the Mexican Foreign Investment Regulations. The Mexican Commission of Foreign Investment and the Mexican Registry of Foreign Investments (the "*Registro Nacional de Inversiones Extranjeras*")

are responsible for the administration of the Foreign Investment Law and the Mexican Foreign Investment Regulations.

As a general rule, the Foreign Investment Law allows foreign investment in up to 100% of the capital stock of Mexican companies except for those engaged in certain specified restricted industries. Foreign investment in our capital stock is restricted.

Under the Federal Telecommunications Law and the Foreign Investment Law, basic telephony concessions may be granted only to:

- Mexican individuals; and
- Mexican corporations in which non-Mexicans own 49% or less of the full voting stock and that are not otherwise controlled by non-Mexicans.

However, in the case of concessions for cellular telecommunications services, foreign investment participation may exceed 49% of the voting stock with the prior approval of the Mexican Foreign Investment Bureau of the Mexican Ministry of Economy (*Secretaría de Economía*).

Pursuant to the Foreign Investment Law, the Mexican Ministry of Economy may also authorize the issuance of nonvoting or limited voting stock (also known as “neutral shares”) that are not counted for purposes of determining the foreign investment percentage of a Mexican corporation under the Mexican Foreign Investment Law. Any share transfers resulting in a violation of these foreign ownership requirements are invalid under Mexican law.

Forfeiture of Shares

As required by Mexican law, our bylaws provide that, upon acquiring our shares, non-Mexican shareholders agree (i) to be considered as Mexicans with respect to their shares as well as to the property, rights, concessions, participations or interests owned by us or to the rights and obligations derived from any agreements that we may have with the Mexican federal government and (ii) not to invoke the protection of their own government. If a shareholder should invoke such governmental protection in violation of this agreement, their shares would be forfeited to the Mexican federal government. This prohibition does not apply to actions before courts of law of foreign countries.

Submission to Jurisdiction

Our bylaws provide that in connection with any controversy between our shareholders and us, or between our shareholders in connection with any matter related to us, both we and our shareholders shall submit to the jurisdiction of the courts of Monterrey, Nuevo León, Mexico.

C. Material Contracts

Exhibit 4.16 - acquisition of Avantel,

Exhibit 4.17 - Avantel and Telmex Agreements,

Exhibit 4.18 - Bridge Credit Agreement, and

Exhibit 4.19 - Term Loan Agreement.

D. Exchange Controls

There are currently no exchange controls in Mexico.

E. Taxation

Income tax rate in Mexico is 28%. Mexican regulations allow companies to deduct tax losses against income tax, potentially reducing tax payments. All interest payments we make under the senior notes, the bridge loan, the syndicated term loan and all other existing indebtedness with a foreign counterpart, are made free and clear of and without deduction or withholding taxes.

F. Dividends and Paying Agents

Not applicable.

G. Statement by Experts

Not applicable.

H. Documents on Display

Where You May Find More Information

We file reports and other information with the SEC. You may review copies of any documents that we file with the SEC, including their exhibits and schedules, at the SEC's public reference room at 450 Fifth Street, N.W., Room 1024, Washington, D.C. 20549. You may also get copies of all or any portion of the documents that we file from the public reference room, the regional offices or by calling the SEC at 1-800-SEC-0330 or by writing the SEC, upon payment of a prescribed fee. Our SEC filings are also available to you on the SEC's web site at <http://www.sec.gov>.

I. Subsidiary Information

Not applicable.

Item 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company and its subsidiaries are exposed, by their normal business relations, to some financial risks denominated as rate risks and currency exchange rate risks, principally. To mitigate the exposure to those risks the Company and its subsidiaries use financial derivative instruments.

By using derivative financial instruments to hedge exposures to changes in currency exchange rates fluctuations, the Company exposes itself to credit risk and market risk. Credit risk is the failure of the counterparty to perform under the terms of the derivative contract. When the fair value of a derivative contract is positive, the counterparty owes the Company, which creates credit counterparty risk for the Company. When the fair value of a derivative contract is negative, the Company owes the counterparty and, therefore, it does not possess credit risk. The Company minimizes the credit risk in derivative instruments by entering into transactions with high-quality foreign financial counterparties.

In the operations with financial derivative instruments that are registered as hedging activities we establish a hedging program, in which the Company and its subsidiaries formally establish the objective of the hedging, the strategy of administration of risks, the instrument of hedging, or the transaction covered, the nature of the risk that its being hedged, how the effectiveness of the financial instrument will be proved to compensate the risk covered and the methodology to measure the effectiveness of hedging.

The Company and its subsidiaries realize proves of effectiveness, prospective and retrospective, to watch in every moment that the relations of hedging keep a high effectiveness according to accounting standards. At the moment that ineffectiveness is detected the Company will register that amount in the results as part of the CFR.

Financial derivative instruments registered with hedging purposes

According to the accounting models for hedging activities that are permitted by financial standards, the dimension, risks and estimated impact in balance sheet or income statement of the following financial derivative instruments are presented below. Contrarily to financial instruments with trading purposes, the derivatives with hedging purpose will not generate volatility in the income statement, as long as they accomplish in all the term, with the requirements of the financial standards to keep the classification of hedging activities:

Fair value hedge

- a) On March 22, 2007, the Company contracted a CCS (Currency Swap) to cover the risk of exchange rate generated by the syndicated term loan for U.S. \$110.2 million in which the Company will receive payments of 3 month Libor plus 150 basis points over U.S. \$110.2 million notional and will pay a monthly rate of TIE 28 days plus 135 basis points over Ps. 1,215,508 notional which includes the amortizations of principal. This transaction is under the fair value hedge accounting model.

Maturity date	Currencies		Interest Rates		
	Notional amount (USD)	Notional amount (MXP)	Axtel receives	Axtel pays	Estimated fair value
February 29, 2012	<u>U.S. \$ 110.23</u>	<u>Ps. 1,216</u>	Libor + 1.5	TIE + 1.35	<u>U.S. \$(2.4)</u>

For the year ended December 31, 2007 the change in the fair value of the hedging activity of the syndicated term loan resulted in an unrealized loss amount of U.S.\$3.1 million recognized in the comprehensive financial result, compensated by the change in the fair value of the debt valued at December 31, 2007 in U.S.\$2.9 million.

Cash flow hedge

- a) On March 29, 2004, the Company entered into a derivative a Ps-USD CCS to hedge a portion of its U.S. dollar foreign exchange exposure resulting from the issuance of the U.S. \$175 million 11% senior notes, which matures in 2013. Under this CCS transactions, Axtel will receive semiannual payments calculated based on the aggregate notional amount of U.S. \$113.75 million at an annual U.S. rate of 11%, and the Company will make semiannual payments calculated based on the aggregate of Ps.1,270,019 (nominal value) at annual rate of 12.30%.
- b) Derived from the reopening of the issuance on March 2005 for U.S. \$75 million and as a complement of the hedge strategy mentioned above, on June 6, 2005, the Company entered into a new derivative a Ps-USD CCS. The purpose of this agreement was to hedge the remaining portion of its U.S. dollar foreign exchange exposure resulting from the first issuance, and the totality of its U.S. \$75 million issuance. Under this agreement, Axtel will receive semiannual payments calculated based on the aggregate notional amount of U.S. \$136.25 million at an annual rate of 11%, and the Company will make semiannual payments calculated based on the aggregate of Ps.1,480,356 (nominal value) at annual rate of 12.26%.
- c) On February 3, 2007, the Company entered into a new derivative IOS ("Interest Only Swap"). The purpose of this agreement was to hedge the debt service from its new U.S. dollar bond issuance. Under this agreement, Axtel will receive semiannual payments calculated based on the aggregate notional amount of U.S. \$275 million at a fixed annual rate of 7.625%, and the Company will make semiannual payments calculated based on the aggregate of Ps.3,038,750 (nominal value) at a fixed annual rate of 8.54%.

As of December 31, 2007, the CCS information is as follows:

(Amounts in charts are expressed in millions)

Maturity date	Currencies		Interest Rates		
	Notional amount (USD)	Notional amount (nominal value) (MXP)	Axtel receives (USD)	Axtel pays (MXP)	Estimated Fair Value
Dec 15, 2008	U.S. \$ 113.75	Ps. 1,270	11.00%	12.30%	U.S.\$ (1.6)
Dec 15, 2008	U.S. \$ 136.25	Ps. 1,480	11.00%	12.26%	U.S.\$ (1.5)
Feb 1, 2012	U.S. \$ 275.00	Ps. 3,039	7.86%	8.54%	U.S.\$ (4.2)

For the year ended December 31, 2007, the change in the fair value of these CCS is an unrealized loss amount of U.S. \$1.7 million. This gain was recognized within the other comprehensive income section of equity, net of deferred taxes.

Derivatives registered as trading

The Company does not enter into any financial derivative instrument with any other purpose but hedging. The Company does not speculate using financial instruments.

However, the Company redeemed 35% of the issuance of U.S. \$250 million derived from the issuances of debt of December, 2003 and March, 2005. In the face of this situation and originated by the closing of Swaps described in sections a) and b) from the paragraph “Cash flow hedges”, the Company stayed with an “over-hedge” in these derivatives therefore it decided to cover this excess of hedge with an inverse operation, having the volatility of this portion being registered in the CFR. This operation is a CCSS (Currency Swap), in this transaction the Company receives 12.26% over a notional amount of Ps. 950.7 million and pays 11% over the notional amount of U.S. \$87.5 million. According to the financial reporting standards this Swap does not comply with the requirements to be registered as a risk hedge; however it is considered as an economic hedge by the Company. The CCS information is as follows:

(Amounts in charts are expressed in millions)

Maturity date	Currencies		Interest Rates		
	Notional amount (USD)	Notional amount (MXP)	Axtel receives (USD)	Axtel pays (MXP)	Estimated fair value
December 15, 2008	U.S. \$ 87.50	Ps. 950.7	12.26%	11.0%	U.S. \$0.9

For the year ended December 31, 2007 the added value of U.S. \$1.0 million of this operation was registered in the comprehensive financial result.

Embedded derivatives

The Company has conducted an initiative to identify, analyze and segregate if applicable, those contractual terms and clauses that implicitly or explicitly embed derivatives characteristics within financial or non financial agreements. These instruments are commonly known as embedded derivatives and do follow the same accounting treatment as of those free-standing contractual derivatives. Based on the above, the Company identified and recognized an amount of Ps. 1,261 from embedded derivatives effects during 2007 in the accounting records..

Item 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES

Not applicable.

Part II

Item 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES

Not applicable.

Item 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS

Not applicable.

Item 15. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures.

We maintain a set of disclosure controls and procedures designed to provide reasonable assurance that information required to be disclosed by the Company in report that it files or submits under the U.S. Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

An evaluation was carried out under the supervision and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures as of December 31, 2007. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective.

Management's Annual Report on Internal Control over Financial Reporting.

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in the rules promulgated under the Exchange Act. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Because of its inherent limitations, internal control over financial reporting is not intended to provide absolute assurance that a misstatement of our financial statements would be prevented or detected.

Under the supervision and with the participation of our management, including our Chief Executive Officer and principal financial and accounting officers, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in "Internal Control – Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). The evaluation included a review of the documentation of controls, evaluation of the design effectiveness of controls, and testing of the operating effectiveness of controls.

Based on this evaluation, our management concluded that internal control over financial reporting was effective as of December 31, 2007.

Item 16A. AUDIT COMMITTEE FINANCIAL EXPERT

Our Board of Directors has determined that Mr. Bernardo Guerra Treviño has the attributes of an “audit committee financial expert” as defined by the SEC. See “Item 6A. Directors and Senior Management.”

Item 16B. CODE OF ETHICS

We have established a code of ethics that applies to our Chief Executive Officer, Chief Financial Officer, principal accounting officer and other corporate and divisional employees. [However, our board of directors has not, as of yet made a determination whether modification of our code of ethics will be required to comply with SEC requirements.] We will provide to any person without charge, upon request, a copy of such code of ethics. Such requests shall be made in writing to the attention of Adrian de los Santos at Axtel, S.A.B. de C.V., Blvd. Gustavo Diaz Ordaz 3.33 No. L-1, Col. Unidad San Pedro, San Pedro Garza Garcia, N.L., Mexico, CP 66215.

Item 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES

KPMG Cardenas Dosal S.C. (“KPMG”) served as our auditors for the years ended December 31, 2007 and 2006. The following table sets forth the fees paid to KPMG for the financial years ended December 31, 2007 and 2006.

	Year ended December 31	
	2007	2006
	(in millions of nominal pesos)	(in millions of nominal pesos)
Audit Fees (1)	Ps. 5.9	Ps. 4.5
Tax Fees (2)	0.5	0.2
All Other Fees (3)(4)	1.3	1.4
Total Fees	<u>7.7</u>	<u>6.1</u>

- (1) Audit fees include fees associated with the annual audit of our consolidated financial statements. Audit fees also include fees associated with various audit requirements relating to SEC filing requirements.
- (2) Tax fees include fees principally incurred for assistance with VAT reimbursements and compliance matters.
- (3) Audit related fees include fees associated with audit and revisions needed regarding the acquisition of Avantel.
- (4) Introduction to bulletin C-10.

We have introduced procedures for the review and pre-approval of any services performed by KPMG. The procedures require that all proposed engagements of KPMG for audit and permitted non-audit services are submitted to the audit committee for approval prior to the beginning of any such services.

The audit committee selects the company’s auditor on an annual basis. The auditor presents a detail business plan which is reviewed and agreed by the company, and occasionally complemented with additional activities requested by the management or the Board of Directors. Every year, the company performs an evaluation of the auditors’ prestige, experience, fairness, position among the top 4 auditing firms and the economic proposal is within market standards, among others. Once the company has made this evaluation and agreed on the auditors business plan, the management recommends the auditing firm to the audit committee.

We did not have an audit committee prior to January 2004.

Item 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES

Not applicable.

Item 16E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS

Not applicable.

Part III

Item 17. FINANCIAL STATEMENTS

The Company has responded to Item 18 in lieu of this item.

Item 18. FINANCIAL STATEMENTS

See pages F-1 through F-[].

Item 19. EXHIBITS

Exhibit Number Description

1.1	Corporate By-laws (Estatutos Sociales) of Axtel, S.A. de C.V. (“Axtel”), together with an English translation (incorporated herein by reference to Exhibit 3.1 of our Registration Statement on Form F-4, File No. 333-114196)
1.2	English summary of Amended Corporate By-laws (Estatutos Sociales) and Articles of Incorporation of Axtel, S.A.B de C.V.
2.1	Indenture, dated as of December 16, 2003, among Axtel, the Subsidiary Guarantors named therein and The Bank of New York, as Trustee, governing Axtel’s \$175,000,000 aggregate principal amount of 11% Senior Notes due 2013 (incorporated herein by reference to Exhibit 4.1 of our Registration Statement on Form F-4, File No. 333-114196).
2.2	Specimen Global Note representing Axtel’s 11% Senior Notes due 2013 (incorporated herein by reference to Exhibit 4.2 of our Registration Statement on Form F-4, File No. 333-114196).
2.3	Form of Specimen Global Note representing the exchange notes (incorporated herein by reference to Exhibit 4.3 of our Registration Statement on Form F-4, File No. 333-114196).
2.4	Registration Rights Agreement, dated as of December 16, 2003 among Axtel, the Subsidiary Guarantors named therein and Credit Suisse First Boston LLC (incorporated herein by reference to Exhibit 4.4 of our Registration Statement on Form F-4, File No. 333-114196).
4.1	Unanimous Shareholders Agreement, dated as of October 6, 1997, among Bell Canada International (Mexico Telecom) Limited, Telinor Telefonía, S.A. de C.V. (“Telinor”), Worldtel Mexico Telecom Ltd. And Axtel (formerly known as Telefonía Inalambrica Del Norte, S.A. de C.V.) (incorporated herein by reference to Exhibit 9.1 of our Registration Statement on Form F-4, File No. 333-114196).
4.2	Joinder Agreement, dated as of March 20, 2003, among Axtel and Nortel Networks Limited (incorporated herein by reference to Exhibit 9.2 of our Registration Statement on Form F-4, File No. 333-114196).

Exhibit Number Description

4.3	Concession title granted by the Mexican Ministry of Communications and Transportation (the “Ministry”) in favor of Axtel (formerly known as Telefonía Inalambrica Del Norte, S.A. de C.V.), dated June 17, 1996, together with an English translation of such concession title (incorporated herein by reference to Exhibit 10.1 of our Registration Statement on Form F-4, File No. 333-114196).
4.4	Amendment, dated December 19, 2002, of concession title granted by the Ministry in favor of Axtel, dated June 17, 1996, together with an English translation of such amendment (incorporated herein by reference to Exhibit 10.2 of our Registration Statement on Form F-4, File No. 333-114196).
4.5	Concession title granted by the Ministry in favor of Axtel, dated October 7, 1998, together with an English translation of such concession title (incorporated herein by reference to Exhibit 10.3 of our Registration Statement on Form F-4, File No. 333-114196).
4.6	Concession title granted by the Ministry in favor of Axtel, dated April 1, 1998, together with an English translation of such concession title (incorporated herein by reference to Exhibit 10.4 of our Registration Statement on Form F-4, File No. 333-114196).
4.7	Concession title granted by the Ministry in favor of Axtel, dated June 4, 1998, together with an English translation of such concession title (incorporated herein by reference to Exhibit 10.5 of our Registration Statement on Form F-4, File No. 333-114196).
4.8	Engagement Letter, dated as of May 15, 2002, by and among Axtel and The Blackstone Group L.P. (incorporated herein by reference to Exhibit 10.6 of our Registration Statement on Form F-4, File No. 333-114196).
4.9	Restructuring Agreement, dated as of March 20, 2003 by and among Axtel, Nortel Networks Limited, Nortel Networks de Mexico, S.A. de C.V. and Toronto Dominion (Texas), Inc. (incorporated herein by reference to Exhibit 10.7 of our Registration Statement on Form F-4, File No. 333-114196).
4.10	Master Agreement for the Provision of Local Interconnection Services, dated as of February 25, 1999, entered into by and between Telefonos de Mexico, S.A. de C.V., Telefonía Inalambrica Del Norte, S.A. de C.V. (predecessor company to Axtel, S.A. de C.V.) (incorporated herein by reference to Exhibit 10.9 of our Registration Statement on Form F-4, File No. 333-114196).
4.11	Technical Assistance Support Services Agreement for FWA Equipment, dated as of March 20, 2003, among Nortel Networks UK Limited and Axtel (incorporated herein by reference to Exhibit 10.11 of our Registration Statement on Form F-4, File No. 333-114196).
4.12	FWA Technology License Agreement, dated as of March 20, 2003, among Nortel Networks Limited and Axtel (incorporated herein by reference to Exhibit 10.12 of our Registration Statement on Form F-4, File No. 333-114196).
4.13	FWA Special Agreement, dated as of September 30, 2003, among Nortel Networks UK Limited and Axtel (incorporated herein by reference to Exhibit 10.13 of our Registration Statement on Form F-4, File No. 333-114196).

Exhibit Number Description

4.14	Purchase and License Agreement for FWA Equipment and the Technical Assistance Support Services Agreement for FWA Equipment, dated as of December 28, 2004, between Airspan Communications Limited and Axtel (incorporated herein by reference to Exhibit 10.13 of our Registration Statement on Form F-4, File No. 333-123608) (certain portions of Exhibit 10.12 have been omitted <input type="checkbox"/> pursuant to a request for confidential treatment).
4.15	Amendment No.3 to the Technical Assistance Support Services Agreement for FWA Equipment, dated as of December 28, 2004, between Airspan Communications Limited and Axtel (incorporated herein by reference to Exhibit 10.13 of our Registration Statement on Form F-4, File No. 333-123608) (certain portions of Exhibit 10.13 have been omitted pursuant to a request for confidential treatment).
4.16	Summary of Avantel acquisition documents (Master Agreement, Asset Purchase Agreement, Partnership Interest Purchase Agreement)
4.17	Summary of Avantel agreement entered into with Telmex and Telnor (Long Distance Interconnection Agreement, Agreement for 800 numbers access toll free service, Local Interconnection Agreement, Settlement Agreement, Capacity Lease Agreement)
4.18	Bridge Credit Agreement entered into with Credit Suisse, Cayman Islands Branch, acting as the Administrative Agent, various financial institutions and Axtel on November 30, 2006
4.19	Term Loan Agreement entered into with Citibank, N.A. as the Administrative Agent and Banco Nacional de México, S.A. Integrante del Grupo Financiero Banamex, as the Peso Agent, various Financial Institutions, and Axtel on November 30, 2006
7.1	Statement regarding computation of ratio of earnings to fixed charges (according to Mexican GAAP) (incorporated herein by reference to Exhibit 12.1 of our Registration Statement on Form F-4, File No. 333-114196).
7.2	Statement regarding computation of ratio of earnings to fixed charges (according to U.S. GAAP) (incorporated herein by reference to Exhibit 12.2 of our Registration Statement on Form F-4, File No. 333-114196).
8.1	List of Subsidiaries of Axtel (incorporated herein by reference to Exhibit 21.1 of our Registration Statement on Form F-4, File No. 333-114196).
8.2	Amended list of Axtel Subsidiaries including the Avantel companies.
12.1	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
12.2	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

Audited Consolidated Financial Statements

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SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

Axtel, S.A.B. de C.V.

/s/ Patricio Jimenez Barrera
Patricio Jimenez Barrera
Chief Financial Officer

April 25, 2008

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Consolidated Financial Statements

December 31, 2007

(With comparative figures for 2006 and 2005)

(With Report of Independent Registered Public Accounting
Firm)



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64650 Monterrey, N.L.

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Fax: + 01 (81) 83 33 05 32
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Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Axtel, S.A.B. de C.V.:


We have audited the accompanying consolidated balance sheets of Axtel, S.A.B. de C.V. and subsidiaries (the Company) as of December 31, 2007 and 2006, and the related consolidated statements of operations, changes in stockholders' equity, and changes in financial position for each of the years in the three-year period ended December 31, 2007. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States) and auditing standards generally accepted in Mexico. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement and are prepared in accordance with Mexican Financial Reporting Standards. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the reporting standards used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Axtel, S.A.B. de C.V. and its subsidiaries as of December 31, 2007 and 2006, and the consolidated results of their operations, the changes in their stockholders' equity and the changes in their financial position for each of the years in the three-year period ended December 31, 2007, in conformity with Mexican Financial Reporting Standards.

Mexican Financial Reporting Standards vary in certain significant respects from U.S. generally accepted accounting principles information relating to the nature and effect of such differences is presented in note 25 to the consolidated financial statements.

KPMG Cárdenas Dosal, S.C.


Leandro Castillo Parada

Monterrey, N.L., México
February 25, 2008, except for note 24
which is as of April 23, 2008 and note 25
which is as of April 29, 2008

KPMG Cárdenas Dosal, S.C. la firma Mexicana miembro
de KPMG International, una cooperativa Suiza.

Aguascalientes, Ags.
Cancún, Q. Roo.
Chihuahua, Chih.
Ciudad Juárez, Chih.
Culiacán, Sin.
Guadalajara, Jal.
Hermosillo, Son.
Mérida, Yuc.
Mexicali, B.C.

México, D.F.
Monterrey, N.L.
Puebla, Pue.
Querétaro, Qro.
Reynosa, Tamps.
Saltillo, Coah.
San Luis Potosí, S.L.P.
Tijuana, B.C.
Toluca, Edo. de Mex.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Consolidated Balance Sheets**

(Thousands pesos of constant purchasing power as of December 31, 2007)

Assets	December 31,	
	2007	2006
Current assets:		
Cash and cash equivalents	Ps. 1,573,877	1,222,145
Accounts receivable (note 7)	1,822,349	1,660,560
Refundable taxes and other accounts receivable	113,148	252,662
Prepaid expenses	45,657	43,862
Inventories (note 10)	167,889	103,070
Total current assets	3,722,920	3,282,299
Long-term accounts receivable	18,254	20,686
Property, systems and equipment, net (notes 11 and 16)	13,679,871	14,036,601
Intangible assets (note 14)	1,058,204	1,422,814
Pre-operating expenses, net (note 12)	111,897	159,591
Deferred income taxes (note 19)	936,089	620,877
Deferred employee's profit sharing (note 19)	14,180	27,774
Investment in shares of associated company (note 13)	15,249	14,127
Other assets, net (note 15)	274,013	309,207
Total assets	Ps. <u>19,830,677</u>	<u>19,893,976</u>
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	Ps. 1,848,934	1,919,175
Accrued interest	111,849	16,446
Taxes payable	136,556	62,624
Current maturities of long-term debt (note 16)	160,163	163,207
Other accounts payable (note 17)	394,006	511,205
Deferred revenue (note 9)	583,052	614,551
Derivative financial instruments (note 8)	93,861	68,541
Total current liabilities	3,328,421	3,355,749
Long-term debt, excluding current maturities (note 16)	7,484,955	8,294,282
Other long-term accounts payable	6,215	3,014
Severance, seniority premiums and other post retirements benefits (note 18)	57,514	85,506
Deferred revenue (note 9)	203,226	271,103
Total liabilities	<u>11,080,331</u>	<u>12,009,654</u>
Stockholders' equity (note 20):		
Common stock	8,870,062	8,677,782
Additional paid-in capital	741,671	547,131
Deficit	(949,610)	(1,440,606)
Cumulative deferred income tax effect	132,168	132,168
Change in the fair value of derivative instruments (note 8)	(43,945)	(32,153)
Total stockholders' equity	8,750,346	7,884,322
Commitments and contingencies (note 22)		
Total liabilities and stockholders' equity	Ps. <u>19,830,677</u>	<u>19,893,976</u>

The accompanying notes are an integral part of the consolidated financial statements.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Consolidated Statements of Operations

For the years ended December 31, 2007, 2006 and 2005

(Thousands pesos of constant purchasing power as of December 31, 2007)

		Years ended December 31,		
		2007	2006	2005
Telephone services and related revenues (note 21)	Ps.	12,190,610	6,675,712	5,362,393
Operating costs and expenses:				
Cost of revenues and services		(4,504,713)	(2,104,361)	(1,673,995)
Selling and administrative expenses		(3,601,427)	(2,260,105)	(1,821,849)
Depreciation and amortization		(2,690,687)	(1,560,054)	(1,220,253)
		<u>(10,796,827)</u>	<u>(5,924,520)</u>	<u>(4,716,097)</u>
Operating income		<u>1,393,783</u>	<u>751,192</u>	<u>646,296</u>
Comprehensive financing result:				
Interest expense		(925,049)	(482,735)	(411,207)
Interest income		134,441	92,135	61,275
Foreign exchange gain, net		972	23,700	112,129
Change in the fair value of derivative instruments		19,942	(24,808)	-
Monetary position gain		<u>268,797</u>	<u>11,467</u>	<u>58,733</u>
Comprehensive financing result, net		<u>(500,897)</u>	<u>(380,241)</u>	<u>(179,070)</u>
Employee's profit sharing (note 19)		(6,088)	(1,570)	-
Deferred employee's profit sharing (note 19)		(13,594)	4,699	-
Other (expenses) income, net		<u>(438)</u>	<u>(35,770)</u>	<u>7,735</u>
Other (expenses) income, net		<u>(20,120)</u>	<u>(32,641)</u>	<u>7,735</u>
Income before income taxes and equity in results of associated company		872,766	338,310	474,961
Income tax expense (note 19)		(98,819)	(4,894)	-
Deferred tax expense (note 19)		(284,381)	(112,656)	(167,881)
Total income tax expense		<u>(383,200)</u>	<u>(117,550)</u>	<u>(167,881)</u>
Equity in earnings of associated company (note 13)		1,430	1,652	-
Net income	Ps.	<u>490,996</u>	<u>222,412</u>	<u>307,080</u>
Weighted average common shares outstanding		8,754,493,119	8,522,810,598	8,522,810,598
Basic and diluted earnings per share (pesos)	Ps.	<u>0.06</u>	<u>0.03</u>	<u>0.04</u>

The accompanying notes are an integral part of the consolidated financial statements.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Consolidated Statements of Changes in Financial Position

For the years ended December 31, 2007, 2006 and 2005

(Thousands pesos of constant purchasing power as of December 31, 2007)

		Years ended December 31,		
		2007	2006	2005
Operating activities:				
Net income	Ps.	490,996	222,412	307,080
Add charges (deduct credits) to operations not requiring (providing) resources:				
Depreciation		2,299,574	1,413,288	1,098,350
Amortization		391,113	146,766	121,903
Accrual for seniority premiums and severance		11,324	12,474	8,233
Deferred income tax and employee's profit sharing		297,975	107,957	167,881
Equity in earnings of associated company		(1,430)	(1,652)	-
Resources provided by operations		3,489,552	1,901,245	1,703,447
(Investment in) net financing from operations		(262,804)	630,851	(179,342)
Resources provided by operating activities		3,226,748	2,532,096	1,524,105
Financing activities:				
Increase in common stock		192,280	-	751,832
Additional paid-in capital		194,540	(9,804)	400,108
(Payments) proceeds from loans, net		(812,371)	5,409,926	612,213
Restricted cash		-	37,225	(37,225)
Accrued interest		95,403	2,680	1,633
Other accounts payable		11,523	8,986	(3,485)
Resources (used in) provided by financing activities		(318,625)	5,449,013	1,725,076
Investing activities:				
Acquisition and construction of property, systems and equipment, net		(2,486,093)	(7,854,529)	(1,767,092)
Pre-operating expenses		-	(13,991)	(11,049)
Investment in shares of associated company		-	(12,474)	-
Intangible assets		-	(752,082)	-
Other assets		(70,298)	(167,551)	(47,687)
Resources used in investing activities		(2,556,391)	(8,800,627)	(1,825,828)
Increase (decrease) in cash and cash equivalents		351,732	(819,518)	1,423,353
Cash and cash equivalents at beginning of year		1,222,145	2,041,663	618,310
Cash and cash equivalents at end of year	Ps.	1,573,877	1,222,145	2,041,663

The accompanying notes are an integral part of the consolidated financial statements.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Consolidated Statements of Changes in Stockholders' Equity

For the years ended December 31, 2007, 2006 and 2005

(Thousands pesos of constant purchasing power as of December 31, 2007)

		Common stock	Additional paid-in capital	Deficit	Cumulative deferred income tax effect	Change in the fair value of derivative instruments	Total stockholders' equity
Balances as of December 31, 2004	Ps.	7,925,950	156,827	(1,970,098)	132,168	(333)	6,244,514
Issuance of common stock (note 20a)		751,832	400,108	-	-	-	1,151,940
Comprehensive income (note 20c)		<u>-</u>	<u>-</u>	<u>307,080</u>	<u>-</u>	<u>(62,428)</u>	<u>244,652</u>
Balances as of December 31, 2005		8,677,782	556,935	(1,663,018)	132,168	(62,761)	7,641,106
Issuance costs		-	(9,804)	-	-	-	(9,804)
Comprehensive income (note 20c)		<u>-</u>	<u>-</u>	<u>222,412</u>	<u>-</u>	<u>30,608</u>	<u>253,020</u>
Balances as of December 31, 2006		8,677,782	547,131	(1,440,606)	132,168	(32,153)	7,884,322
Issuance of common stock (note 20a)		192,280	194,540	-	-	-	386,820
Comprehensive income (note 20c)		<u>-</u>	<u>-</u>	<u>490,996</u>	<u>-</u>	<u>(11,792)</u>	<u>479,204</u>
Balances as of December 31, 2007	Ps.	<u>8,870,062</u>	<u>741,671</u>	<u>(949,610)</u>	<u>132,168</u>	<u>(43,945)</u>	<u>8,750,346</u>

The accompanying notes are an integral part of the consolidated financial statements.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Thousands pesos of constant purchasing power as of December 31, 2007)

(1) Basis of presentation

On February 25, 2008, the Administration of the Company authorized the issuance of the accompanying consolidated financial statements and related footnotes.

According to Mexican General Corporation Law and the Company statutes, the stockholders' have the right to change the financial statements after their issuance. The accompanying financial statements will have to be approved at the next Stockholders' Meeting.

The accompanying consolidated financial statements have been prepared in accordance with Mexican Financial Reporting Standards (FRS).

(2) Organization, description of business and salient events

Axtel, S.A.B. de C.V. and subsidiaries (the Company or AXTEL) is a Mexican corporation engaged in operating and/or exploiting a public telecommunication network to provide voice, sound, data, text, and image conducting services, and local, national, and international long-distance calls. To provide these services and carry out the Company's activity, a concession is required (see note 22e). In June 1996, the Company obtained a concession from the Mexican Federal Government to install, operate and exploit public telecommunication networks for an initial period of thirty years.

AXTEL offers different access technologies, including fixed wireless access, point-to-point, point-to-multipoint radio links, WiMAX, fiber optic and copper technology, which are used depending on the communication needs of the clients.

On August 31, 2007, the stockholders' approved a three-for-one stock split (the split). The split became effective on October 8, 2007. The proportional equity interest participation of existing stockholders did not change as a result of the split. For comparison purposes, the number of shares in note 20 have been adjusted for the effects of the split for all periods presented.

On February 2, 2007, the Company issued U.S. \$275 million of 10-year unsecured senior notes. This issuance matures on February 1, 2017. The interest will be payable semiannually and the senior notes bear interest at $7\frac{5}{8}\%$ beginning on August 1, 2007. The proceeds of this issuance were used to prepay the bridge financing related to the December 2006 acquisition of Avantel (see note 16).

As described in note 20, on January 4, 2007 Telecomunicaciones Holding Mx, S. de R.L. de C.V. ("Tel Holding") subscribed and paid 246,453,963 Series B shares (represented by 35,207,709 CPOs) through the Instituto Nacional de Valores ("INDEVAL"), in relation to the subscription agreement.

As described in note 5, on November 27, 2006 the Company signed an agreement with Banco Nacional de Mexico, S.A. ("Banamex") and Tel Holding to acquire all the assets and shares of Avantel Infraestructura, S. de R.L. de C.V. and Avantel, S. de R.L. de C.V. therefore the results of operations have been included in the Company's consolidated statement of operations since December 1, 2006. As described in note 16 the acquisition transaction was financed through various loans amounting to approximately U.S. \$515 million.

On February 22, 2006 the Company redeemed U.S. \$87,500,000 aggregate principal amount of its 11% senior notes due 2013, or 35% of the U.S. \$250,000,000 original aggregate principal amount of the notes.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Thousands pesos of constant purchasing power as of December 31, 2007)

The redemption was made at a price of 111% of the principal amount of the notes, plus accrued and unpaid interest through the redemption date. The premium paid on this transaction amounted to approximately U.S. \$9.6 million, and is included in the statement of operations as part of the comprehensive financing result. In relation with this transaction, deferred financing cost amounting to Ps. 28,441 were amortized.

(3) Summary of significant accounting policies

The accounting policies and practices followed by the Company in the preparation of the consolidated financial statements are described below:

(a) Use of estimates

The preparation of consolidated financial statements requires management of the Company to make a number of estimates and assumptions relating to the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include the carrying amount of property, plant and equipment, valuation allowances for receivables, inventories and deferred income tax assets; valuation of derivative instruments; and assets and obligations related to employee benefits. Actual results could differ from these estimates and assumptions.

For purposes of disclosure in the notes to the consolidated financial statements, references to pesos or "Ps.", are to Mexican pesos; likewise, references to dollars or U.S. \$, are to dollars of the United States of America.

(b) Recognition of the effects of inflation

The accompanying consolidated financial statements have been prepared in accordance with Financial Reporting Standards in Mexico (FRS), which include the recognition of the effects of inflation on the financial information, and are expressed in thousands of Mexican pesos at the constant purchasing power of December 31, 2007 based upon the National Consumer Price Index (NCPI) published by Banco de Mexico. The indexes used in recognizing the effects of inflation were as follows:

	NCPI	Inflation %
December 2007	459.101	3.76
December 2006	442.468	4.05
December 2005	425.232	3.30

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Thousands pesos of constant purchasing power as of December 31, 2007)

(c) *Principles of consolidation*

The consolidated financial statements include the financial statements of Axtel and the subsidiaries mentioned below. All accounts and intercompany transactions have been eliminated in the preparation of the consolidated financial statements. The consolidation was made based on audited financial statements of each of the subsidiaries, which were prepared in accordance with FRS.

The Company owns, directly or indirectly, 100% of the following subsidiaries:

Subsidiary	Main activity
Instalaciones y Contrataciones, S. A. de C. V. ("Icosa")	Administrative services
Impulsora e Inmobiliaria Regional, S. A. de C. V. ("Inmobiliaria")	Property management
Servicios Axtel, S. A. de C. V. ("Servicios Axtel")	Administrative services
Avantel, S. de R.L. de C.V. ("Avantel")*	Telecommunications services
Avantel Infraestructura S. de R.L. de C.V. ("Avantel Infraestructura")*	Telecommunications services
Adequip, S.A.	Fiber optic rings leasing
Avantel Recursos, S.A. de C.V. ("Recursos")	Administrative services
Avantel Servicios, S.A. de C.V. ("Servicios")	Administrative services
Telecom. Network, Inc. ("Telecom")	Telecommunications services

* On June 30, 2005, Avantel Infraestructura and certain subsidiaries as partners, together with Avantel as a representative partner of the Joint Venture, entered into a Joint Venture agreement to permit Avantel provide services and operate Avantel Infraestructura's public telecommunications network. Under this agreement, Avantel Infraestructura contributed the concessioned network, and the other associates contributed the customer agreements, as well as support and human resources services.

As a result of the above, Avantel Infraestructura entered into an agreement with Avantel to transfer the concession rights granted by the Secretaria de Comunicaciones y Transportes ("SCT").

(d) *Cash equivalents*

Cash equivalents of Ps. 1,390,858 and Ps. 948,961 at December 31, 2007 and 2006, respectively, consist of overnight repurchase agreements and certificates of deposit with an initial term of less than three months. Cash equivalents are carried at the lower of acquisition cost plus accrued interest as of the most recent balance sheet date or net estimated realizable value. Interest and foreign currency exchange fluctuation are included in the statements of operations as part of the comprehensive financing result.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Thousands pesos of constant purchasing power as of December 31, 2007)

(e) *Trade accounts receivable*

Trade accounts receivable includes the amount billed to customers and a provision for services rendered at the balance sheet date but not billed. Amounts billed are recorded at the invoiced amount and do not bear interest. The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in the Company's existing accounts receivable. The Company reviews its allowance for doubtful accounts monthly. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential recovery is considered remote.

(f) *Investment in shares of associated company*

The investment in shares of associated company is accounted by the equity method when AXTEL has the ability to exercise significant influence but does not control the associated company. The ability to exercise significant influence is presumed where AXTEL owns more than 20%, but less than 50% of the voting shares of an associated company. AXTEL's investments in associated companies are carried in the balance sheet at an amount that reflects AXTEL's share of the net assets of the associates.

(g) *Inventories and cost of sales*

Inventories are carried at the lower of restated cost and net realizable value and are accounted using the average cost method. The restated cost is determined by application of the NCPI factor to current costs.

(h) *Property, systems and equipment*

Property, systems and equipment are recorded at acquisition cost and restated by NCPI factors. Property under capital leases are stated at the present value of minimum lease payments.

Starting January 1, 2007, the acquisitions of assets in period of construction or installation include the corresponding comprehensive financing result as part of the assets value.

Comprehensive financing results incurred up to June 1999 during construction or installation periods were capitalized as part of the cost of the assets that were acquired during the pre-operating stage. Since that date, comprehensive financing results have been recognized as part of the results of the year in which they are incurred.

Depreciation of property, systems and equipment is calculated using the straight-line method, based on useful lives estimated by management. Useful lives are described in note 11.

Leasehold improvements are amortized over the shorter of the useful life of the improvement or the lease term.

Maintenance and repairs, including the cost of replacing minor items not constituting substantial betterments are expensed as incurred and charged principally to selling and administrative expenses.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Thousands pesos of constant purchasing power as of December 31, 2007)

(i) Telephone concession rights

Telephone concession rights that are included within intangible assets, are restated by NCPI factors and amortized under the straight-line method over a period of 20 to 30 years (the initial term of the concession rights). Avantel's telephone concession rights are amortized over the remaining term of life.

(j) Pre-operating expenses

Pre-operating expenses include administrative services, technological advice and comprehensive financing results incurred through June 1999 and also the expenses incurred during 2000, 2004, 2005 and 2006 in opening offices in other cities throughout the country. These expenses were capitalized, and restated by NCPI factors and are amortized under the straight-line method over a period of 10 years (see note 12).

(k) Other and intangible assets

Other assets mainly include costs related to Telmex / Telnor infrastructure costs and notes issuance costs. Other assets also include guarantee deposits and, beginning 2005, the intangible asset related to the labor obligations (see note 15). These assets are restated by NCPI factors and amortized on a straight-line basis.

As a consequence of the acquisition of Avantel and based upon calculations prepared by an independent expert appraiser, the Company recognized intangible assets as follows: trade name, customer relationships and concession rights (see note 14).

(l) Seniority premiums, severance payments and post employment benefits

Seniority premium benefits, and, beginning 2005, severance compensation for reasons other than restructuring, to which employees are entitled in accordance with the Federal Labor Law are charged to expense based on actuarial computations of the present value of this obligation. Amortization of prior service costs is based on the estimated average service lives of existing personnel. As of December 31, 2007, the average service life of employees entitled to plan benefits approximates 16 years.

(m) Derivative financial instruments

The Company accounts for derivatives and hedging activities in accordance with Bulletin C-10 for Mexican GAAP and FASB Statement No. 133, for US GAAP, "Accounting for Derivate Instruments and Certain Hedging Activities," as amended (FAS 133), which require that all derivative instruments be recorded on the balance sheet date at their respective fair values, including those derivatives embedded in financial or non financial contractual agreements.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Thousands pesos of constant purchasing power as of December 31, 2007)

The Company uses financial derivative instruments in order to manage financial exposures, especially risks associated with foreign currency and interest rates. In accordance with Bulletin C-10 and FAS 133, the Company may apply hedge accounting to such instruments if it meets certain requirements and assesses whether the derivatives that are used in hedging transactions are highly effective in offsetting cash flows of hedged items. The Company accounts for the financial derivative instruments designated as hedging activities into two main classifications: (i) Fair value hedging and (ii) Cash flows hedging.

In addition, the Company has accounted for certain financial derivative instruments under the classification of trade, that did not meet the requirements for hedge accounting at fair value in the balance sheet with changes in fair value recognized directly in the income statement, even though these instruments are highly effective.

For financial derivative instruments that are designated as fair value hedges, the changes in the fair value of those instruments and the changes in the fair value of the hedged item are recorded in the income statement. Changes in the fair value of financial derivative instruments that are highly effective and that are designated and qualify as cash flow hedges are recorded in comprehensive income to the extent that the derivative is effective as a hedge, until earnings are affected by the variability of the designated hedged item.

The ineffectiveness portion of the change in the fair value of a derivative instrument that qualifies as a hedge is reported in the income statement.

The Company will discontinue hedge accounting prospectively when it is determined that the derivative is no longer effective in offsetting changes in the fair value or cash flows of the hedged item, the derivative expires or is sold, terminated, or exercised. In all situations in which hedge accounting is discontinued and the derivative is retained, the Company continues to carry the derivative at its fair value on the balance sheet and recognizes any subsequent changes in the fair value of the financial instrument directly in the income statement. When it is probable that a forecasted transaction will not occur, the Company discontinues hedge accounting and recognizes immediately in earnings gains and losses that were accumulated in comprehensive income (see note 8).

(n) *Income tax (IT), tax on assets (TA) and employee's statutory profit sharing (ESPS)*

IT is accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Deferred ESPS is recognized for timing differences arising from the reconciliation of book income to income for profit sharing purposes with respect to which it may reasonably be estimated that a future liability or benefit will arise and there is no indication that the liabilities or benefits will not materialize.

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(Thousands pesos of constant purchasing power as of December 31, 2007)

(o) *Inflation adjustment of common stock, other contributions and deficit*

This adjustment is determined by multiplying stockholder contributions and deficit by NCPI factors, which measure accumulated inflation from the dates contributions were made and losses arising through the most recent year end. The resulting amounts represent the constant value of stockholders' equity.

(p) *Comprehensive income (loss)*

The comprehensive income (loss) represents the net income or loss for the year plus the effect of those items reflected directly in stockholders' equity, other than capital contributions, reductions and distributions.

(q) *Cumulative deferred income tax effect*

This amount represents the cumulative effects of deferred taxes as of the date of adoption of the FRS D-4.

(r) *Comprehensive financing result (CFR)*

The CFR includes interest income and expense, foreign exchange gain and loss, the monetary position gain and valuation effects of financial instruments, less the amounts capitalized, as part of property, systems and equipment and pre-operating expenses.

Foreign currency transactions are recorded at the rate of exchange prevailing on the date of execution or settlement. Foreign currency assets and liabilities are translated at the exchange rate in force at the balance sheet date. Exchange differences arising from assets and liabilities denominated in foreign currencies are recognized in the results of operations.

Monetary position gains and losses are determined by multiplying the difference between monetary assets and liabilities at the beginning of each month, including the deferred taxes, by inflation factors through year-end. The aggregate of these results represents the monetary gain or loss for the year arising from inflation, which is recognized in the CFR.

(s) *Revenue recognition*

The Company's revenues are recognized when the service has been provided and the collection for such service is reasonably assured, as follows:

- *Telephony Services* –The Company generates revenue by enabling our customers to originate and receive an unlimited number of calls. Customers are charged a flat monthly fee for basic service, a per call fee for local calls ("measured service"), a per minute usage fee for calls completed on a cellular line ("calling party pays" or "CPP calls") and national and international long distance calls, and a monthly fee for value-added services and internet services when requested by the customer. The costs related to the termination of our customers' cellular and long distance calls on other carriers' networks are charged to cost in the same month that the revenue is earned.

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Notes to Consolidated Financial Statements

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- *Activation* - At the moment of installing the service when the customer has a contract with indefinite term; otherwise is recognized according to the term of the contract between the customer and the Company.
- *Equipment*. At the moment of selling the equipment and when the customer acquires the property of the equipment and assumed all risks.
- *Integrated services*. At the moment when the client receives the service.

Other costs and expenses related to sales and marketing, costs of leasing land related to our operations and maintenance of the network, billing, payment processing, operator services and our leasing of private circuit links are recorded as incurred.

(t) *Business and risk concentration*

The Company rendered services to one client that represents approximately 11%, 16% and 17% of total net rental, installation, service and other revenues during 2007, 2006 and 2005, respectively. The Company provides an allowance for doubtful accounts based on management's analyses and estimations. The allowance expense is included as selling and administrative expenses in the consolidated statement of operations.

(u) *Contingencies*

Liabilities for loss contingencies are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated. When a reasonable estimation can not be made, qualitative disclosure is provided in the notes to the consolidated financial statements. Contingent revenues, earnings or assets are not recognized until their realization is virtually assured.

(v) *Impairment of property, systems and equipment and other non-current assets*

The Company evaluates, at least once a year, the adjusted values of its property, systems and equipment and other non-current assets subject to amortization to determine whether there is an indication of potential impairment or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed off are separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated.

(w) *Segment information*

The Company believes that it operates in one business segment. Management does view the business as consisting of two revenues streams (Mass market and Business Market); however it is not possible to attribute direct or indirect costs to the individual streams other than selling expenses.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Thousands pesos of constant purchasing power as of December 31, 2007)

(4) Accounting changes

The FRS B-3, *Statement of Income*, issued by the Mexican Board for Research and Development of Financial Reporting Standards (Consejo Mexicano para la Investigación y Desarrollo de Normas de Información Financiera or CINIF) became effective beginning January 1, 2007. Accordingly, the accompanying statement of income for 2006, has been modified for reporting as provided under this FRS, which together with the Interpretation of Financial Reporting Standards (INIF) 4, modified the general rules for the presentation and structure of the statement of income, eliminating the special and extraordinary items classifications, and requiring that the employee statutory profit sharing be reported under other expenses and income, rather than being presented in a line following tax on earnings, and additionally requiring that income, costs and expenses be classified as follows:

- i) Ordinary – Those related to the entity’s line of business, i.e., those arising from or inherent to its primary activities, representing the principal sources of revenue, whether frequent or not.
- ii) Non-ordinary – Those arising from activities which do not represent the entity’s principal sources of revenue, which are generally infrequent.

In addition, this FRS requires that ordinary costs and expenses be classified based on their nature, function, or a combination of both. Since the Company is a service entity, ordinary costs and expenses are classified in order to present a clearer understanding of the financial information.

FRS D-6, “*Capitalization of the Comprehensive Financial Results (CFR)*”, issued by the CINIF, became effective for the fiscal year beginning January 1, 2007. This FRS establishes the requirement to capitalize CFR attributable to certain assets having an extended acquisition period prior to being put into use. The effects of adopting this FRS are disclosed in note 11.

(5) Acquisition of Avantel

On November 27, 2006, the Company signed an agreement with Banamex, and Tel Holding, former controlling stockholders of Avantel, to purchase substantially all of the assets of Avantel Infraestructura, S. de R.L. de C.V. (“Avantel Infraestructura”) for U.S. \$485 million. The Company also agreed to purchase the equity interests of Avantel Infraestructura and Avantel, S. de R.L. de C.V. (“Avantel Concesionaria,” both companies together being referred to as “Avantel”) and each of Avantel’s subsidiaries for U.S. \$31 million. After obtaining all required approvals from AXTEL’s stockholders and government regulators, the Company completed the acquisition on December 4, 2006. The operating results of Avantel are included in the consolidated financial statements of the Company from the date of purchase.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Thousands pesos of constant purchasing power as of December 31, 2007)

(a) Description of Avantel

Avantel Concesionaria and Avantel Infraestructura are affiliated companies and participate in a joint venture. Through this vehicle, the companies offer services of local telephony, domestic and international long distance and data services in Mexico.

Avantel provides telecommunication services to business, government and residential customers in Mexico. Avantel is Mexico's second largest provider of domestic and international long distance telephone services based on revenues and, recently, has increased its participation in the Internet and data transmission markets. Avantel operates a fiber optic network of approximately 7,700 kilometers that reaches over 200 cities in Mexico.

Avantel is one of the leading providers of Internet-Protocol (IP) solutions in Mexico. Avantel's IP solutions are especially tailored to meet the diverse needs of companies of all sizes and sectors, and their scope ranges from intelligent voice and data transmission to virtual private networks, or VPN's, integrated telecommunications packages and managed services.

(b) Transaction objective

The main objective of the transaction is to create an added value for the stockholders of the Company through the projected benefits of synergies, more strength by increasing the size of the Company, more presence on nation wide coverage and more efficiency for the expansion in new cities, among others, which will traduce in an increase of our competitive advantages that Axtel keeps against its actual and future competitors.

(c) Purchase price allocation

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed as of the acquisition date. The acquisition cost of Avantel was approximately U.S. \$520 million (Ps. 5,928,967). This amount includes certain costs and expenses associated with the transaction, such as financial advisory costs, lawyers, independent experts of valuation, among others.

After the recognition of the effects of FRS B-7, an excess in the value of the net assets acquired over the cost of the transaction was recognized of approximately Ps. 1,157,926, and following the rules of the FRS B-7, the excess was proportionally applied to reduce the property, systems and equipment and intangible assets.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Thousands pesos of constant purchasing power as of December 31, 2007)

As of November 30, 2007, the effect of the assets acquired and liabilities assumed after the adjustments made during 2007 are as follows:

<u>Balance Sheet:</u>	<u>Preliminary Value</u>	<u>Adjustments</u>	<u>Definitive Value</u>
Current assets	Ps. 1,242,121	-	1,242,121
Property, systems and equipments, net	6,568,961	(597,333)	5,971,628
Intangible assets	831,100	(122,870)	708,230
Deferred income tax	748,093	595,007	1,343,100
Others	84,604	-	84,604
Total of assets acquired	9,474,879	(125,196)	9,349,683
Current liabilities	2,455,832	(107,687)	2,348,145
Long term liabilities	867,201	(17,509)	849,692
Total of liabilities assumed	3,323,033	(125,196)	3,179,837
Net assets acquired	Ps. <u>6,151,846</u>	<u>-</u>	<u>6,151,846</u>

As of December 31, 2006 the revenues and costs of Avantel that were included in the consolidated financial statements amounted to Ps. 689,835 and Ps. 567,793, respectively.

The main adjustments are detailed as follows:

- Property, systems and equipment: The additional adjustments during the period were related with the final appraisal realized by independent experts, cancellation of systems that will not be used anymore and will be replaced by systems of Axtel and the effects of the of negative goodwill.
- Intangible assets: The additional adjustments during the period were related with the final appraisal realized by independent experts and the effects of the negative goodwill.
- Deferred income taxes: The adjustments were related mainly to the cancellation of reserves of tax loss carryforwards from Avantel subsidiaries for better results than they were expected in 2006, and the effect derived from the other adjustments mentioned above.
- Current liabilities: These adjustments correspond to the elimination of the accrual created in connection to the early termination of links leased by Avantel. The terminated contracts did not have any cost associated.
- Long-term liabilities: This adjustment corresponds to the cancellation of the pension plan as mentioned in note 18.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Thousands pesos of constant purchasing power as of December 31, 2007)

(d) Pro forma financial information

We derived the summary unaudited pro forma financial information from our consolidated financial statements of Axtel, S.A.B. de C.V. and Subsidiaries and the combined financial statements of Avantel Infraestructura, S. de R.L. de C.V. and Subsidiaries and Avantel, S. de R.L. de C.V. adjusted to give effects to the purchase method of accounting for the acquisition described above and the results of operations as through the combination had been completed at the beginning of 2005 and 2006.

The Company provides the unaudited pro forma financial information for informational purposes only. They do not purport to indicate the operating results or financial position that would have been achieved if the acquisition had occurred on the assumed dates, nor do they purport to indicate our future operating results or financial position.

The unaudited consolidated pro forma financial information is as follows:

		Years ended December 31:	
		2006	2005
		<u>(Unaudited)</u>	<u>(Unaudited)</u>
Revenues	Ps.	12,202,687	11,701,269
Costs of revenues and services		(4,917,435)	(4,873,823)
Selling and administrative expenses		(3,782,407)	(3,931,166)
Depreciation and amortization		(2,676,745)	(2,513,591)
Operating income		826,100	382,687
Net income (loss)		10,527	(113,052)
Earnings (loss) per share		0.00	(0.04)

(6) Foreign currency exposure

Monetary assets and liabilities denominated in dollars as of December 31, 2007 and 2006 are as follows:

		(Thousands of dollars)	
		<u>2007</u>	<u>2006</u>
Current assets		125,138	120,606
Current liabilities		(82,750)	(85,125)
Long-term liabilities		<u>(552,826)</u>	<u>(587,343)</u>
Foreign currency liability position, net		<u>(510,438)</u>	<u>(551,862)</u>

The U.S. dollar exchange rates as of December 31, 2007 and 2006 were Ps. 10.86 and Ps. 10.88, respectively. As of February 25, 2008, the exchange rate was Ps. 10.80 to \$1.

As of December 31, 2007, the Company had foreign exchange derivative instruments (see note 8).

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Thousands pesos of constant purchasing power as of December 31, 2007)

As of December 31, 2007 and 2006, the Company had the following non-monetary assets of foreign origin, the replacement cost of which may only be determined in dollars:

	(Thousands of dollars)	
	<u>2007</u>	<u>2006</u>
Inventories	11,602	4,154
Systems and equipment, gross	<u>1,172,351</u>	<u>1,164,437</u>
	<u><u>1,183,953</u></u>	<u><u>1,168,591</u></u>

Following is a summary for the years ended December 31, 2007, 2006 and 2005, of transactions carried out with foreign entities, excluding imports and exports of systems and equipment:

	(Thousands of dollars)		
	<u>2007</u>	<u>2006</u>	<u>2005</u>
Telephone services	79,996	7,505	-
Interest expense	61,493	34,569	30,869
Commissions	6	21	223
Administrative and technical advisory services	4,107	1,336	1,311
Cost of services	<u>1,115</u>	<u>591</u>	<u>-</u>
	<u><u>146,717</u></u>	<u><u>44,022</u></u>	<u><u>32,403</u></u>

(7) Accounts receivable

Accounts receivable consist of the following:

	<u>2007</u>	<u>2006</u>
Trade	Ps. 3,188,094	2,880,468
Less allowance for doubtful accounts	<u>1,365,745</u>	<u>1,219,908</u>
Accounts receivable, net	Ps. <u><u>1,822,349</u></u>	<u><u>1,660,560</u></u>

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

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The activity in the allowance for doubtful accounts for the years ended December 31, 2007, 2006 and 2005 was as follows:

		<u>2007</u>	<u>2006</u>	<u>2005</u>
Balances at beginning of year	Ps.	1,175,711	179,043	100,219
Bad debt expense		190,034	119,563	78,873
Write-offs		-	(13)	(49)
Avantel		<u>-</u>	<u>877,118</u>	<u>-</u>
Balances at end of year not adjusted for inflation		1,365,745	1,175,711	179,043
Effects of inflation		<u>-</u>	<u>44,197</u>	<u>14,260</u>
Balances at year end at constant pesos	Ps.	<u>1,365,745</u>	<u>1,219,908</u>	<u>193,303</u>

(8) Derivative instruments and hedging activities

The Company and its subsidiaries are exposed, by their normal business relations, to some financial risks such as interest rate risks and foreign exchange rate risks, principally. To mitigate the exposure to those risks, the Company and its subsidiaries use financial derivative instruments.

By using derivative financial instruments to hedge exposures to foreign exchange rate fluctuations, the Company exposes itself to credit risk and market risk. Credit risk is the failure of the counterparty to perform under the terms of the derivative contract. When the fair value of a derivative contract is positive, the counterparty owes the Company, which creates credit counterparty risk for the Company. When the fair value of a derivative contract is negative, the Company owes the counterparty and, therefore, it does not possess credit risk. The Company minimizes the credit risk in derivative instruments by entering into transactions with high-quality foreign financial counterparties.

For financial derivative instruments that are designated as hedging activities, the Company and its subsidiaries formally document the hedging relationship and its risk management objective and strategy for undertaking the hedge, the hedging instrument, the hedged item, the nature of the risk being hedged, how the hedging instrument's effectiveness in offsetting the hedged risk will be assessed and the methodology to measure the ineffectiveness.

The Company and its subsidiaries assess, prospectively and retrospectively, at inception and on an ongoing basis whether the derivatives used in hedging transactions are highly effective according to accounting standards. The ineffective portion of the change in fair value of a derivative instrument is recorded in the results as part of the CFR.

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Financial derivative instruments designated as hedges

According to the accounting models for hedging activities that are permitted by financial accounting standards, the dimension, risks and estimated impact in the balance sheet or income statement of the following financial derivative instruments are presented below. Contrarily to financial instruments with trading purposes, the derivatives designated as hedges will not generate volatility in the income statement, as long as the instruments are highly effective and continue to meet the financial accounting standards to keep the classification as hedging activities:

Fair value hedge

- a) On March 22, 2007, the Company contracted a CCS (Currency Swap) to cover the risk of exchange rate generated by the syndicated term loan for U.S. \$110.2 million in which the Company will receive payments of 3 month Libor plus 150 basis points over U.S. \$110.2 million notional and will pay a monthly rate of TIIE 28 days plus 135 basis points over Ps. 1,215,508 notional which includes the amortizations of principal. This transaction is under the fair value hedge accounting model.

(Amounts in charts are expressed in million)

Maturity date	Currencies		Interest Rates		
	Notional amount (USD)	Notional amount (MXP)	Axtel receives	Axtel pays	Estimated fair value
February 29, 2012	<u>U.S. \$ 110.23</u>	<u>Ps. 1,216</u>	Libor + 1.5 TIIE +1.35		<u>U.S. \$(2.4)</u>

For the year ended December 31, 2007 the change in the fair value of the hedging activity of the syndicated term loan resulted in an unrealized loss amount of U.S. \$3.1 million recognized in the comprehensive financial result, compensates by the change in the fair value of the debt valued at December 31, 2007 in U.S. \$2.9 million.

Cash flow hedge

- a) On March 29, 2004, the Company entered into a derivative a Ps-USD CCS to hedge a portion of its U.S. dollar foreign exchange exposure resulting from the issuance of the U.S. \$175 million 11% senior notes, which matures in 2013. Under this CCS transactions, Axtel will receive semiannual payments calculated based on the aggregate notional amount of U.S. \$113.75 million at an annual U.S. rate of 11%, and the Company will make semiannual payments calculated based on the aggregate of Ps. 1,270,019 (nominal value) at annual rate of 12.30%.

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- b) Derived from the reopening of the issuance on March 2005 for U.S. \$75 million and as a complement of the hedge strategy mentioned above, on June 6, 2005, the Company entered into a new derivative a Ps-USD CCS. The purpose of this agreement was to hedge the remaining portion of its U.S. dollar foreign exchange exposure resulting from the first issuance, and the totality of its U.S. \$75 million issuance. Under this agreement, Axtel will receive semiannual payments calculated based on the aggregate notional amount of U.S. \$136.25 million at an annual rate of 11%, and the Company will make semiannual payments calculated based on the aggregate of Ps. 1,480,356 (nominal value) at annual rate of 12.26%.
- c) On February 3, 2007, the Company entered into a new derivative IOS ("Interest Only Swap"). The purpose of this agreement was to hedge the debt service from its new U.S. dollar bond issuance. Under this agreement, Axtel will receive semiannual payments calculated based on the aggregate notional amount of U.S. \$275 million at a fixed annual rate of 7.625%, and the Company will make semiannual payments calculated based on the aggregate of Ps. 3,038,750 (nominal value) at a fixed annual rate of 8.54%.

As of December 31, 2007, the CCS information is as follows:

(Amounts in charts are expressed in million)

Maturity date	Currencies		Interest Rates		
	Notional amount (USD)	Notional amount (nominal value) (MXP)	Axtel receives (USD)	Axtel pays (MXP)	Estimated fair value
December 15, 2008	U.S. \$ 113.75	Ps. 1,270	11.00%	12.30%	U.S.\$ (1.6)
December 15, 2008	U.S. \$ 136.25	Ps. 1,480	11.00%	12.26%	U.S.\$ (1.5)
February 1, 2012	U.S. \$ 275.00	Ps. 3,039	7.86%	8.54%	U.S.\$ (4.2)

For the year ended December 31, 2007, the change in the fair value of these CCS is an unrealized loss amount of U.S. \$1.7 million. This gain was recognized within the other comprehensive income section of equity, net of deferred taxes.

Derivatives designated as trading

The Company only enters into financial derivative instrument that it intends to mitigate a forecasted transaction or the unpredictability of cash flows to be received or paid related to a recognized asset or liability. The Company does not speculate using financial instruments.

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However, the Company redeemed 35% of the issuance of U.S. \$250 million derived from the issuances of debt of December, 2003 and March, 2005. In the face of this situation and originated by the closing of Swaps described in sections a) and b) from the paragraph "Cash flow hedges", the Company stayed with an "over-hedge" in these derivatives therefore it decided to cover this excess of hedge with an inverse operation having the volatility of this portion being registered in the CFR. This operation is a CCSS (Currency Swap), in this transaction the Company receives 12.26% over a notional amount of Ps. 950.7 million and pays 11% over the notional amount of U.S. \$87.5 million. According to the financial reporting standards this Swap does not comply with the requirements to be registered as a risk hedge, however it is considered as an economic hedge by the Company. The CCS information is as follows:

(Amounts in charts are expressed in million)

Maturity date	Currencies		Interest Rates		
	Notional amount (USD)	Notional amount (MXP)	Axtel receives (MXP)	Axtel pays (USD)	Estimated fair value
December 15, 2008	U.S. \$ 87.50	Ps. 950.7	12.26%	11.0%	U.S. \$0.9

For the year ended December 31, 2007 the added value of U.S. \$1.0 million of this operation was registered in the comprehensive financial result.

Embedded derivatives

The Company has conducted an initiative to identify, analyze and segregate if applicable, those contractual terms and clauses that implicitly or explicitly embed derivatives characteristics within financial or non financial agreements. These instruments are commonly known as embedded derivatives and do follow the same accounting treatment as of those free-standing contractual derivatives. Based on the above, the Company identified and recognized an amount of Ps. 1,261 from embedded derivatives effects during 2007 in the accounting records.

(9) Related parties transactions

The main transactions with related parties, during the years ended December 31, 2007, 2006 and 2005 are as follows:

	2007	2006	2005
Telephone services	Ps. 595,055	94,309	-
Commissions and administrative services Banamex	19,490	5,801	-
Interest expense	146,894	12,757	-
Commissions for debt restructure	-	41,016	-
Lease expense	24,198	24,452	46,845
Banamex deferred revenue	437,918	724,767	-
Installations services expense	7,429	6,425	6,238
Others	2,594	-	9,692

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During December 2006, Avantel received from Banamex approximately U.S. \$40 million in relation to diverse contracts of services between them. One of the contracts is to provide services of technical support on site during 60 months and the second contract consists in the prepayment of 13 months of recurring telephony services for three years. During 2007, Avantel received from Banamex approximately U.S. \$39 million in relation to the contract of the prepayment of 13 months of recurring telephony services.

In 2005, the Company entered into a service agreement for marketing and advertising inside a theme park.

In March and May 2000, the Company entered into a lease agreement with Gemini, S.A. de C.V. for the lease of land and property on which the corporate offices and certain infrastructure are located.

In April 2002, the Company signed a service agreement with Instalaciones y Desconexiones Especializadas, S.A. de C.V. for the provision of installation services with regard to customer premise equipment.

The due from and due to balances with related parties as of December 31, 2007 and 2006 are as follows:

	<u>2007</u>	<u>2006</u>
Due from:		
Operadora de Parques y Servicios, S.A. de C.V.	Ps. <u>1,996</u>	<u>4,942</u>
	<u>2007</u>	<u>2006</u>
Due to:		
GEN Industrial, S.A. de C.V.	Ps. 45	-
Instalaciones y Desconexiones Especializadas, S.A. de C.V.	329	-
Neoris de Mexico, S.A. de C.V.	<u>8,423</u>	<u>-</u>
Total	Ps. <u>8,797</u>	<u>-</u>

As of December 31, 2007 the Company has debt with Citibank, N.A. and Banamex, S.A. as described in note 16.

(10) Inventories

Inventories consist of the following:

	<u>2007</u>	<u>2006</u>
Telephones and caller identification devices	Ps. 17,308	32,643
Installation material	18,653	10,220
Tools	11,240	9,164
Network spare parts	54,313	35,613
Other	<u>66,375</u>	<u>15,430</u>
Total inventories	Ps. <u>167,889</u>	<u>103,070</u>

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(11) Property, systems and equipment

Property, systems and equipment are as follows:

		<u>2007</u>	<u>2006</u>	<u>Useful lives</u>
Land	Ps.	162,100	168,202	
Building		344,377	355,908	25 years
Computer and electronic equipment		1,849,492	1,542,930	3 years
Transportation equipment		88,791	107,764	4 years
Furniture and fixtures		138,060	120,733	10 years
Network equipment		18,070,984	16,376,096	6 to 28 years
Leasehold improvements		244,930	198,324	5 to 14 years
Construction in progress		1,475,384	1,130,535	
Advances to suppliers		19,646	28,501	
		<u>22,393,764</u>	<u>20,028,993</u>	
Less accumulated depreciation		<u>8,713,893</u>	<u>5,992,392</u>	
Property, systems and equipment, net	Ps.	<u>13,679,871</u>	<u>14,036,601</u>	

The Company has capitalized CFR in construction in progress as a complement of the acquisition cost, for an accumulated amount of Ps. 13,006, as of December 31, 2007. The CFR capitalized during 2007 amounted to Ps. 10,545. During 2006 the Company did not capitalized CFR.

(12) Pre-operating expenses, net

The capitalized pre-operating expenses incurred up to June 1999 and expenses incurred during 2000, 2004, 2005 and 2006 in opening new operations are as follows:

		<u>2007</u>	<u>2006</u>
Salaries	Ps.	231,963	231,963
Legal and financial advisory		118,238	118,238
Operating expenses		96,649	96,649
Depreciation		10,275	10,275
Comprehensive financing result		(25,929)	(25,929)
Service and other revenues		(14,657)	(14,657)
Other		40,880	40,880
		<u>457,419</u>	<u>457,419</u>
Less accumulated amortization		<u>345,522</u>	<u>297,828</u>
Pre-operating expenses, net	Ps.	<u>111,897</u>	<u>159,591</u>

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(13) Investment in shares of associated company

As of December 31, 2007 and 2006, the investment in shares of associated company through Avantel is represented by a non-controlling 50% interest in the equity shares of Conectividad Inalámbrica 7GHZ, S. de R.L. (Conectividad Inalámbrica). The operation of this company consists in providing radio communication services in Mexico under the concession granted by the SCT. Such concession places certain performance conditions and commitments to this company, such as (i) filing annual reports with the SCT, including identifying main stockholders of the Company, (ii) reporting any increase in common stock, (iii) providing continuous services with certain technical specifications, (iv) to present a code of marketing strategies, (v) to register rates of service, (vi) to provide a bond and (vii) fulfilling the program of investments presented when the company solicited the concession.

Since the Company does not have effective control, this investment is accounted for under the equity method.

Condensed financial information of the associated company as of December 31, 2007 and 2006 is as follows:

Balance Sheet:

	<u>2007</u>	<u>2006</u>
Current assets	Ps. 12,972	7,955
Intangible assets	17,586	20,909
Total assets	30,558	28,864
Total liabilities	60	611
Stockholders' equity	Ps. 30,498	28,253
50% equity interest	Ps. 15,249	14,127

Statement of operations:

Revenues from rent of frequency bands	Ps. 5,602	503
Costs of services and operating expenses	(2,088)	(151)
Operating income	3,514	352
Comprehensive financial results	(368)	2,953
Deferred income tax	(287)	-
Net income	Ps. 2,859	3,305
Equity in income of associated company	Ps. 1,430	1,652

As of December 31, 2007 and 2006, the liabilities of the Company with Conectividad Inalámbrica were Ps. 5,194 and Ps. 853, respectively.

(14) Intangible assets

Intangible assets consist of the following:

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		<u>2007</u>	<u>2006</u>
Telephone concession rights AXTEL	Ps.	1,073,135	1,073,135
Telephone concession rights Avantel		114,336	150,417
Customer list		324,183	401,111
Trade name "Avantel"		<u>186,074</u>	<u>200,555</u>
		1,697,728	1,825,218
Less accumulated amortization		<u>639,524</u>	<u>402,404</u>
Intangible assets, net	Ps.	<u><u>1,058,204</u></u>	<u><u>1,422,814</u></u>

Concessions rights of the Company

The Company has either obtained concessions as described below to offer telecommunications services or auctioned the following licenses over the spectrum of frequencies necessary to provide the services:

On June, 1996 Axtel obtained a concession to offer local and long distance telephony services, for a period of thirty years. To maintain this concession the Company needs to comply with certain conditions. It can be renewed for another period of thirty years;

- On September 15, 1995 Avantel obtained a concession to offer local and long distance telephony services, for a period of thirty years. To maintain this concession the Company needs to comply with certain conditions. It can be renewed for another period of thirty years;
- Two concessions in 929 MHz to offer mobile paging services;
- 50MHz in the 3.4GHz band. The licenses obtained allow nationwide coverage. The investment was Ps. 831,043 for a period of twenty years with an extension option;
- 56 MHz in the 7 GHz band, countrywide coverage, for a point-to-point transport (through the property of 50% of Conectividad Inalámbrica 7GHz, S. de R.L.);
- 60MHz for Point-to-Multi-Point in the 10.5GHz band nationwide. The acquisition of these twenty-year concessions, with an extension option, represented an investment of Ps. 160,931 for the Company;
- 120 MHz in three regions in 10.5 GHz band, for point-to-multi-point access (Concession originally granted to Avantel);
- 112MHz for Point-to-Point in the 15GHz band and a 100MHz in the 23GHz band, both with nationwide coverage. The acquisition of these twenty-year concessions, with an extension option, represented an investment of Ps. 81,161 for the Company;
- 56 MHz in the 15 GHz band, nationwide coverage, for point-to-point access and transport (Concession originally granted to Avantel);

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- 268 MHz in the 23 GHz band, nationwide coverage, for point-to-point access and transport (Concession originally granted to Avantel);
- 112 MHz in the 37 to 38.6 GHz band, in 5 regions, for point-to-point transport (Concession originally granted to Avantel).

Each license of spectrum has a period of life of 20 years and it can be renovated for additional periods of 20 years as long as Axtel complies with all of its obligations, with all conditions imposed by the law and with any other condition that SCT imposes.

The concessions allow the Company to offer the following services:

- Local telephony service;
- National long distance telephony service;
- Selling or leasing of network capacity for the generation, transmission or reception of data, signs, images, voice, sounds and other type of information of any kind;
- Selling or leasing network capacity from other countries, including the leasing of digital circuits;
- Value added services
- Operator services
- Mobile paging services
- Data services, video, audio conferences and videoconferences, except to restricted TV, continuous services of music or digital audio services; y
- Prepaid phone cards or credit phone cards

In November 2006, SCT granted us, as part of the concession of Axtel, a new permission to provide SMS (short messaging system) to our customers.

Intangible assets from the acquisition of Avantel

Derived from the acquisition of Avantel, the Company recorded certain intangibles assets such as: trade name "Avantel", customer relationships and telephone concession rights, whose value was determined by using independent external expert appraiser in accordance with FRS B-7 and FAS 141. The trade name and the customer relationships that will be amortized over three to five years using the sum of the years' digits method, which we believe best reflects the estimated pattern in which the economic benefits of those relationships will be consumed. The telephone concession right will be amortized over the remaining term of the concession on a straight-line basis.

For the mentioned above intangibles assets we will assess whether any indicators of impairment exist that would trigger a test of any of these definite lived intangible assets, including, but not limited to, a significant decrease in the market price of the asset or cash flows, or a significant change in the extent or manner in which the asset is used. We will also evaluate the remaining useful lives of our definite lived intangible assets each reporting period to determine whether events and circumstances warrant a revision to the

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remaining periods of amortization, which would be addressed prospectively. For example, we review certain trends such as customer churn, average revenue per user, revenue, our future plans regarding the network and changes in marketing strategies, among others.

(15) Other assets

Other assets consist of the following:

		<u>2007</u>	<u>2006</u>
Notes issuance costs	Ps.	143,730	99,533
Deferred financing costs		41,016	89,826
Telmex / Telnor infrastructure costs		68,279	68,279
WTC concession rights		22,474	22,474
Guarantee deposits		35,572	44,737
Other		<u>97,196</u>	<u>49,585</u>
		408,267	374,434
Less accumulated amortization		<u>134,254</u>	<u>65,227</u>
Other assets, net	Ps.	<u><u>274,013</u></u>	<u><u>309,207</u></u>

Notes issuance costs

Notes issuance costs mainly consists of legal and audit fees, documentation, advising, printing, rating agencies, registration fees and out of pocket expenses incurred in relation to the issuance of notes payable and are amortized on a straight line basis over the life of the related debt.

Telmex / Telnor infrastructure costs

As part of the opening of the telecommunications market in Mexico, new telecommunications companies must have interconnection with Teléfonos de Mexico (Telmex) and Teléfonos del Noroeste (Telnor). These two companies made agreements with the new entrants by which they must compensate Telmex and Telnor for their investment in infrastructure that Telmex / Telnor made in order to provide interconnection for the new telephone companies in Mexico.

During 2005, the Company recognized the remaining portion of the amount related to the infrastructure costs. These costs will be amortized on a straight line method over a period of fifteen years, the estimated useful life of this infrastructure.

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Deferred financing costs related with the acquisition of Avantel

The deferred financing costs incurred in the acquisition of Avantel will be amortized based upon the terms of the loans that they are related using the effective interest method.

World Trade Center (WTC) concession rights

Represent the amount paid for obtain concession rights to operate in the WTC building located in Mexico City. This right is amortized over a ten year period which is the length of the agreement.

(16) Long-term debt

Long-term debt as of December 31, 2007 and 2006 consist of the following:

	<u>2007</u>	<u>2006</u>
U.S. \$275,000,000 in aggregate principal amount of 7 ⁵ / ₈ % Senior Unsecured Notes due 2017. Interest is payable semiannually in February 1 and August 1 of each year.	Ps. 2,988,205	-
U.S. \$162,500,000 in aggregate principal amount of 11% Senior Unsecured Notes due 2013. Interest is payable semiannually in arrears on June 15, and December 15 of each year.	1,765,758	1,834,631
Premium on Senior Notes issuance	27,291	32,319
Unsecured Bridge Loan with Credit Suisse, Cayman Island Branch, as the administrative agent, for an aggregate amount of U.S. \$310.9 million, with an interest rate of LIBOR + 125 basis points, maturing in May 2008.	-	3,510,636
Unsecured Syndicated Loan with Citibank, N.A., as the administrative agent, and Banamex as the peso agent, with a peso tranche in the aggregate amount of Ps. 1,042.4 and a U.S. dollar tranche in the aggregate amount of U.S. \$110.2. The final maturity date is February 2012, with quarterly principal repayments starting February 2010, with an interest rate for the tranche in pesos of THIE + 150 basis points, and the tranche in U.S. dollar of LIBOR + 150 basis points.	2,240,091	2,325,992
Change in the fair value of syndicated loan	(31,023)	-
Capacity lease agreement with Teléfonos de Mexico, S.A.B. de C.V. of approximately Ps. 800,000 payable monthly and expiring in 2011.	534,271	593,702
Other long-term financing with several credit institutions with interest rates fluctuating between 6.0% and 7.5% for those denominated in dollars and THIE (Mexican average interbank rate) plus three percentage points for those denominated in pesos.	<u>120,525</u>	<u>160,209</u>
Total long-term debt	7,645,118	8,457,489

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Less current maturities		160,163	163,207
Long-term debt, excluding current maturities	Ps.	<u>7,484,955</u>	<u>8,294,282</u>

Annual installments of long-term debt are as follows:

<u>Year</u>	<u>Amount</u>
2009	Ps. 40,561
2010	1,060,740
2011	1,057,763
2012 and thereafter	<u>5,325,891</u>
	Ps. <u>7,484,955</u>

As of December 31, 2007 and 2006 long-term debt principal characteristics are as follows:

On February 2, 2007, the Company issued U.S. \$275 million of 10-year unsecured senior notes. This issuance matures on February 1, 2017. Interest will be payable semiannually and the senior notes bear interest at $7\frac{5}{8}\%$ beginning on August 1, 2007. The proceeds of this issuance were used to prepay the bridge financing related to the December 2006 acquisition of Avantel.

On December 4, 2006, the Company entered into an Unsecured Bridge Loan Facility with Credit Suisse, Cayman Island Branch, as the Administrative Agent, for an aggregate amount of U.S. \$310,950,000. The bridge loan facility matures eighteen months after the initial drawdown date. With an interest rate of LIBOR +125 basis points. This loan was prepaid on February 2, 2007. Certain subsidiaries of the Company guaranteed this facility.

On December 4, 2006, The Company entered into an Unsecured Credit Agreement with Citibank, N.A. as the Administrative Agent and Banamex as the Peso Agent, and it was modified later on February 23, 2007, with a peso tranche in the aggregate amount of Ps. 1,042,362,416 and a U.S. dollar tranche in the aggregate amount of U.S. \$110,225,133. The credit agreements bear interest rate at LIBOR + 150 basis points for the tranche in U.S. dollar and THIE + 150 basis points for the peso tranche. Avantel, S de R.L. de C.V., Avantel Infraestructura, S. de R.L. de C.V. and Adequip, S.A. guarantee this credit agreement.

On February 22, 2006 the Company redeemed U.S. \$87,500,000 aggregate principal amount of its 11% senior notes due 2013, or 35% of the U.S. \$250,000,000 original aggregate principal amount of the notes. The redemption was made at a price of 111% of the principal amount of the notes, plus accrued and unpaid interest to the redemption date. The premium paid on this transaction was U.S. \$9.6 million, which was recorded in the statement of operations as part of the comprehensive financing result.

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On October 1, 2006, Avantel Infraestructura, S. de R.L. a subsidiary of Axtel S.A.B. de C.V. from December 4, 2006 entered into a capacity lease agreement with Teléfonos de México, S.A.B. de C.V. for purposes of connecting the installations of Avantel and those of Telmex in certain cities by using dedicated links of data for an amount of approximately Ps. 800,000. The monthly lease payment for this contract is approximately Ps. 15 million. The Company evaluated this lease agreement and determined that the present value of the minimum future payments is substantially equal to the market value of the infrastructure and dedicated equipment. Such market value was determined by an independent expert telecommunications appraiser registered within the COFETEL. The Company recorded the lease as a capital lease according to FRS.

Avantel evaluated this lease agreement and determined that the present value of the minimum future payments is substantially equal to the market value of the infrastructure and dedicated equipment. Such market value was determined by an independent expert telecommunications appraiser registered within the COFETEL. Avantel recorded the lease as a capital lease according to FRS D-5.

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Some of the debt agreements that remain outstanding establish certain covenants, the most significant of which refer to limitations on dividend payments and comprehensive insurance on pledged assets. For the year ended December 31, 2007, the Company was in compliance with all of its covenants.

(17) Other accounts payable

As of December 31, 2007 and 2006 other accounts payable consist of the following:

		<u>2007</u>	<u>2006</u>
Guarantee deposits (note 22(a))	Ps.	141,261	146,770
Interest payable (note 22(a))		72,430	58,598
Labor reserves		3,701	122,955
Guarantee deposit (SR Telecom)		69,631	-
Other		<u>106,983</u>	<u>182,882</u>
	Ps.	<u>394,006</u>	<u>511,205</u>

(18) Labor obligations

The cost of the obligations and other elements of seniority premiums, severance payments and pensions mentioned in note 3(l) have been determined based on independent actuarial calculations as of December 31, 2007 and 2006.

The components of the net periodic cost for the years ended December 31, 2007, 2006 and 2005 are as follows:

		2007		2006		2005		
		Seniority Premium	Severance payments	Seniority Premium	Severance payments	Pensions	Seniority Premium	Severance payments
Net periodic cost:								
Labor cost	Ps	1,677	6,019	975	4,156	-	752	4,558
Financial cost	.	281	1,296	151	772	-	106	766
Amortization of transition obligation		1	3,453	1	3,446	-	1	1,649
Variances in assumptions and experience adjustments		(53)	(1,782)	47	72	-	15	-
Inflationary effect		71	359	48	338	-	34	353
Net periodic cost before Avantel's acquisition	Ps	1,977	9,345	1,222	8,784	-	908	7,326
Labor cost of Avantel	.	-	-	46	338	2,085	-	-
Net periodic cost	Ps	1,977	9,345	1,268	9,122	2,085	908	7,326

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The actuarial present value of plan benefit obligations is as follows:

		2007		2006		Pension
		Seniority premium	Severance payments	Seniority premium	Severance payments	
Present benefit obligation	Ps.	10,931	41,429	4,567	24,004	-
Present value of benefits attributable to future salary increases		662	1,843	331	1,075	-
Projected benefit obligation (PBO)		11,593	43,272	4,898	25,079	-
Items pending amortization:						
Variances in assumptions and experience adjustments		(548)	14,631	(1,179)	(3,087)	-
Transition liability		(3)	(11,502)	(5)	(15,059)	-
Minimum additional liability		71	-	852	17,070	-
Net projected liability recognized on the consolidated balance sheet before Avantel's acquisition		11,113	46,401	4,566	24,003	-
Obligations from Avantel's acquisition		-	-	7,757	32,766	35,145
Labor periodic cost		-	-	46	338	2,085
Reclassification to reserve for personal restructuring		-	-	(2,190)	(9,813)	(9,197)
Net projected liability	Ps.	11,113	46,401	10,179	47,294	28,033

The most significant assumptions used in the determination of the net periodic cost of plan are the following:

Discount rate used to reflect the present value of obligations	4.00%	4.00%	4.00% -5.00%	4.00% -5.00%	5.00%
Rate of increase in future salary levels	1.00%	1.00%	0.75% -1.00%	0.75% -1.00%	0.75%
Amortization period of the transition liability	16 years	6 years	17 years	6 years	20.37 years

On May 1, 2007, all the personnel of Avantel Recursos, S.A. de C.V. and Avantel Servicios, S.A. de C.V. were transferred to Servicios Axtel, S.A. de C.V. and Instalaciones y Contrataciones, S.A. de C.V., respectively, transferring with it, all the obligations and rights in labor matters that the personnel had until such date on each of the companies substituted. As part of the standardization of benefits, the pension plan belonging to personnel transferred was concluded.

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(19) Income tax (IT), tax on assets (TA), employee statutory profit sharing (ESPS) and tax loss carryforwards

The parent company and its subsidiaries file their tax returns on a stand-alone basis, and the consolidated financial statements show the aggregate of the amounts determined by each company.

In accordance with the current tax legislation prior to the enactment of the new tax laws in October 2007 described below, companies must pay either the IT or TA, whichever is greater. Both taxes recognize the effects of inflation, in a manner different from financial reporting standards.

On October 1, 2007, new tax laws were published, a number of tax laws were revised, and additionally a presidential decree was issued on November 5, 2007, which was effective on January 1, 2008. The most important changes are: (i) elimination of the Asset Tax Law and (ii) the introduction of a new tax (Flat Rate Business Tax or IETU), which is based on cash flows and limits certain deductions; additionally, certain tax credits are granted mainly with respect to inventories, salaries taxed for IT purposes and social security contributions, tax losses arising from accelerated deductions, recoverable asset tax (AT), and deductions related to investments in fixed assets, deferred charges and expenses. The IETU rate is 16.5% for 2008, 17% for 2009, and 17.5% for 2010 and thereafter.

Accordingly, beginning in 2008, companies will be required to pay the greater of IETU or IT. If, IETU results, the payment will be considered final and not subject to recovery in subsequent years (with certain exceptions).

At December 31, 2007, the Company has evaluated according to Financial Reporting Standards Interpretation (INIF-8 "Efectos del Impuesto Empresarial a Tasa Unica") and after the evaluation, the Company estimated that the tax payable in future years will be IT. Deferred tax effects as of December 31, 2007 have been recorded on the IT basis using a tax rate of 28%.

The TA law establishes a 1.8% tax on assets adjusted for inflation in the case of inventory, property, systems and equipment and net of certain liabilities in accordance with the law. TA levied in excess of IT for the year can be recovered in the succeeding ten years, updated for inflation, provided that in any of such years IT exceeds TA.

Effective January 1, 2002, a new Income Tax Law had been enacted, which provided for a 1% annual reduction in the income tax rate beginning in 2003, so that the income tax rate would have been 32% in 2005. In December 2004, the Mexican Congress approved changes to the Income Tax Law where the tax rate for 2005 was further reduced to 30%. Also, for years 2006 and 2007, the tax rates will decrease to 29% and 28%, respectively. Consequently, the deferred tax assets and liabilities as of December 31, 2007 were calculated using a 28% tax rate. The effects of the reduction in the deferred income tax calculation for 2006 and 2005 were Ps. 12,055 and Ps. 10,924, respectively.

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The income tax expense attributable to the income before IT differed from the amount computed by applying the tax rate of 28% in 2007, 29% in 2006 and 30% in 2005 to pretax income, as a result of the items mentioned below:

		<u>2007</u>	<u>2006</u>	<u>2005</u>
Computed "expected" income tax (expense)	Ps.	(244,374)	(98,110)	(142,488)
(Increase) decrease in income tax expense resulting from:				
Effects of inflation, net		(1,432)	(9,179)	(1,867)
Change in valuation allowance		(101,463)	2,649	(3,346)
Deferred employee's profit sharing		3,806	-	-
Adjustments to deferred tax assets and liabilities for enacted changes in tax rates		-	12,055	10,924
Accelerated tax depreciation effects		(43,550)	(37,688)	-
(Non-deductible expenses) non-taxable income		(5,757)	5,530	(23,473)
Other		9,570	7,193	(7,631)
Income tax expense	Ps.	<u>(383,200)</u>	<u>(117,550)</u>	<u>(167,881)</u>

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities as of December 31, 2007 and 2006 are presented below:

		<u>2007</u>	<u>2006</u>
Deferred tax assets:			
Net operating loss carryforwards	Ps.	968,090	1,426,521
Allowance for doubtful accounts		126,117	84,496
Accrued liabilities		368,420	226,386
Recoverable AT		418,851	332,540
Premium on bond issuance		10,179	12,719
Fair value of derivative instruments		17,090	12,504
Total gross deferred tax assets		1,908,747	2,095,166
Less valuation allowance		530,355	428,892
Net deferred tax assets		<u>1,378,392</u>	<u>1,666,274</u>
Deferred tax liabilities:			
Property, systems and equipment		63,486	507,118
Telephone concession rights		171,848	232,207
Intangible and other assets		206,969	306,072
Total gross deferred tax liabilities		442,303	1,045,397
Net deferred tax assets	Ps.	<u>936,089</u>	<u>620,877</u>

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The rollforward for the net deferred tax asset for the years ended December 31, 2007 and 2006 is presented below:

	<u>2007</u>	<u>2006</u>
Balances at beginning of year	Ps. 620,877	18,562
Deferred IT expense	(284,381)	(112,656)
Deferred IT of derivative financial instruments in stockholders' equity	4,586	(11,903)
Deferred IT from Avantel acquisition	<u>595,007</u>	<u>726,874</u>
Balances at end of year	Ps. <u>936,089</u>	<u>620,877</u>

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax-planning strategies in making this assessment. In order to fully realize the deferred tax asset as of December 31, 2007, the Company will need to generate future taxable income prior to the expiration of the net operating loss carryforwards in various dates as disclosed below. Based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes it is more likely than not that the Company will realize the benefits of these deductible differences, net of the existing valuation allowances at December 31, 2007. The amount of the deferred tax asset considered realizable, however, could be reduced in the near term if estimates of future taxable income during the carryforward period are reduced. As of December 31, 2007, a valuation allowance was primarily established for the deferred tax assets related to TA, tax loss carryforwards of the Company's subsidiaries and allowance for doubtful accounts.

According to the IT law, the tax loss carryforwards and TA carryforwards of each year, restated by inflation, may be carried to the succeeding ten years to offset IT only. As of December 31, 2007, the tax loss carryforwards and recoverable TA expire as follows:

<u>Year</u>	<u>Inflation-adjusted tax loss carryforwards</u>	<u>Recoverable TA</u>
2008	Ps. 1,177,505	-
2009	463,804	-
2010	367,233	-
2011	146,863	70,004
2012	663,555	50,451
2013	454,992	76,966
2014	92,634	72,514
2015	11,489	31,307
2016	75,263	31,298
2017	<u>4,128</u>	<u>86,311</u>
	Ps. <u>3,457,466</u>	<u>418,851</u>

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The tax effects of temporary differences that give rise to deferred employee's profit sharing as of December 31, 2007 and 2006 are presented below:

	<u>2007</u>	<u>2006</u>
Deferred ESPS assets:		
Accrued liabilities	Ps. 2,013	13,793
Accrued for labor obligations	6,554	13,871
Other payroll accruals	<u>7,489</u>	<u>5,526</u>
Net deferred ESPS asset	<u>16,056</u>	<u>33,190</u>
Deferred ESPS liabilities:		
Deferred income	1,876	3,942
Other	<u>-</u>	<u>1,474</u>
Total deferred ESPS liability	<u>1,876</u>	<u>5,416</u>
Deferred ESPS asset, net	Ps. <u>14,180</u>	<u>27,774</u>

The rollforward for the net deferred employee's profit sharing asset for the years ended December 31, 2007 and 2006 is presented below:

	<u>2007</u>	<u>2006</u>
Balances at beginning of year	Ps. 27,774	-
Deferred ESPS (expense) benefit	(13,594)	4,699
Deferred ESPS for acquisition of Avantel	<u>-</u>	<u>23,075</u>
Balances at end of year	Ps. <u>14,180</u>	<u>27,774</u>

Total ESPS expense was calculated from the individual net income of each subsidiary that has employees. The tax profit for ESPS effects of these companies for the year ended December 31, 2007 and 2006 were Ps. 60,880 and Ps. 15,700, respectively.

(20) Stockholders' equity

The principal characteristics of stockholders' equity are described below:

(a) Common stock structure

At December 31, 2007, the Company has 8,769,353,223 shares issued and outstanding. Company's shares are divided in two Series: Series A and B; both Series have two type of classes, Class "I" and Class "II", with no par value. From the total shares, 96,636,627 shares are Series A and 8,672,716.596 shares are Series B. At December 31, 2007 the Company has only issued Class "I" shares. Also, at December 31, 2007 all shares issued are part of the fixed portion.

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On August 31, 2007, the stockholders' approved a three-for-one stock split (the split). The split became effective on October 8, 2007. The proportional equity interest participation of existing stockholders did not change as a result of the split. For comparison purposes, the number of shares is presented adjusted for the effects of the split. Following table shows the effects of the split:

	Number of Shares before the <u>Split</u>	Number of Shares after the <u>Split</u>
Series A Shares	32,212,209	96,636,627
Series B Shares	<u>2,890,905,532</u>	<u>8,672,716,596</u>
Total of Shares	2,923,117,741	8,769,353,223

The percentages of shares holding did not change as a result of the split. For comparability the number of shares have been adjusted for the split in all periods presented.

The following represents a rollforward of Company's shares for the years ended December 31, 2007, 2006 and 2005, after considering the effects of the split:

	Issued and subscribed <u>shares</u>		Common <u>stock</u>	Additional paid-in <u>capital</u>
Balances as of December 31, 2004	7,601,120,598	Ps.	7,925,950	156,827
Shares issued and subscribed	<u>921,690,000</u>		<u>751,832</u>	<u>400,108</u>
Balances as of December 31, 2005	8,522,810,598		8,677,782	556,935
Issuance costs	<u>-</u>		<u>-</u>	<u>(9,804)</u>
Balances as of December 31, 2006	8,522,810,598		8,677,782	547,131
Shares issued and subscribed	<u>246,542,625</u>		<u>192,280</u>	<u>194,540</u>
Balances as of December 31, 2007	<u>8,769,353,223</u>	Ps.	<u>8,870,062</u>	<u>741,671</u>

As of December 31, 2007, the common stock of the Company is Ps. 6,625,536 (nominal value), represented by 96,636,627 common shares, with no nominal value, Class "I", "A" Series, subscribed and paid, and 8,672,716,596 common shares, with no nominal value, Class "I", "B" Series, subscribed and paid.

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In relation to our acquisition of Avantel also included a Series B Shares Subscription Agreement (“Subscription Agreement”) with Tel Holding, an indirect subsidiary of Citigroup, Inc., for an amount equivalent to up to 10% of Axtel’s common stock. To give effect to the above, we obtained stockholder approval (i) to increase our capital by issuing Series B Shares in a number that was sufficient for Tel Holding to subscribe and pay for Series B Shares (in the form of CPOs) representing up to a 10% equity participation in Axtel; and (ii) for the subscription and payment of the Series B Shares that represented the shares subscribed for by Tel Holding and any shares subscribed for by stockholders that elected to subscribe and pay for additional Series B Shares in exercise of their preferential right granted by the Mexican General Corporation Law.

On December 22, 2006 pursuant to the Subscription Agreement, we received a notice from Tel Holding confirming that it acquired 533,976,744 Series B Shares (represented by 76,282,392 CPOs) from the Mexican Stock Exchange (*Bolsa Mexicana de Valores*, or “BMV”) and confirming its intention to subscribe and pay for 246,453,963 new Series B Shares (represented by 35,207,709 CPOs). The new Series B Shares were subscribed and paid for, which we refer to herein as the “Equity Subscription,” by Tel Holding through the CPOs Trust on January 4, 2007. Tel Holding may not, subject to certain exceptions, transfer CPOs purchased in the Equity Subscription until January 3, 2008. The price per share acquired by Tel Holding amounted to Ps. 4.56 per share (nominal value), which was the market value at the date of the subscription.

(b) Stockholders’ equity restrictions

Stockholders’ contributions, restated for inflation as provided in the tax law, totaling Ps. 6,981,059 may be refunded to stockholders tax-free.

No dividends may be paid while the Company has a deficit. Some of the debt agreements mentioned in note 16 establish limitations on dividend payments.

(c) Comprehensive income

The comprehensive income reported on the statements of stockholders’ equity represents the results of the total performance of the Company during the year, and includes the items mentioned below which, in accordance with Mexican FRS, are reported directly in stockholders’ equity, except for net income.

		<u>2007</u>	<u>2006</u>	<u>2005</u>
Net income	Ps.	490,996	222,412	307,080
Fair value of derivative instruments		(16,378)	42,511	(86,832)
Deferred IT of derivative financial instruments		<u>4,586</u>	<u>(11,903)</u>	<u>24,406</u>
Comprehensive income (loss)	Ps.	<u>479,204</u>	<u>253,020</u>	<u>244,652</u>

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(21) Telephone services and related revenues

Revenues consist of the following:

		<u>2007</u>	<u>2006</u>	<u>2005</u>
Local calling services	Ps.	5,336,628	4,330,038	3,770,802
Long distance services		1,532,176	583,605	487,895
Data services		2,513,751	459,063	215,652
International Traffic		1,210,233	552,791	509,266
Other services		<u>1,597,822</u>	<u>750,215</u>	<u>378,778</u>
	Ps.	<u>12,190,610</u>	<u>6,675,712</u>	<u>5,362,393</u>

(22) Commitments and contingencies

As of December 31, 2007, the Company has the following commitments and contingencies:

- (a) On January 24, 2001 a contract was signed with Global Towers Communications Mexico, S. de R.L. de C.V. (Formerly Spectrasite Communications Mexico, S. de R.L. de C.V.) expiring on January 24, 2004, to provide the Company with services to locate, construct, set up and sell sites within the Mexican territory. As part of the operation, the Company agreed to build 650 sites, subject to approval and acceptance by Global Towers Communications Mexico, S. de R.L. de C.V. (Global Towers) and, in turn, sell or lease them under an operating lease plan.

On January 24, 2001, the Company received 13 million dollars from Global Towers to secure the acquisition of the 650 sites at 20,000 dollars per site. These funds are not subject to restriction as per the contract for use and destination. However, the contract provides for the payment of interest at a Prime Rate in favor of Global Towers on the amount corresponding to the number of sites that as of June 24, 2004 had not been sold or leased in accordance with the terms of the contract. The Company has recognized a liability to cover such interest for Ps. 72,430 and Ps. 58,621, respectively, included within other accounts payable in the balance sheet as of December 31, 2007 and 2006, respectively.

During 2002, Global Towers filed an Ordinary Mercantile Trial against the Company before the Thirtieth Civil Court of Mexico City, demanding the refund of the guarantee deposit mentioned above, plus interest and trial-related expenses. The Company countersued Global Towers for unilateral rescission of the contract. As of December 31, 2007, the trial is at a stage where evidence is being shown.

- (b) On December 14, 2007, the Company subscribed an agreement with Metronet, S.A. de C.V., terminating the lawsuit that Metronet filed against the Company. From this date there is neither a contingency nor a liability for this matter.

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- (c) The Company is involved in a number of lawsuits and claims arising in the normal course of business. It is expected that the final outcome of these matters will not have significant adverse effects on the Company's financial position and results of operations.
- (d) In compliance with commitments made in the acquisition of concession rights, the Company has granted surety bonds to the Federal Treasury and to the Ministry of Communication and Transportation amounting to Ps. 1,214 and to other service providers amounting to Ps. 819,648.
- (e) The concessions granted by the Ministry of Communications and Transportation (SCT), mentioned in note 2, establish certain obligations to the Company, including, but not limited to: (i) filing annual reports with the SCT, including identifying main stockholders of the Company, (ii) reporting any increase in common stock, (iii) providing continuous services with certain technical specifications, (iv) filing monthly reports about disruptions, (v) filing the services' tariff, and (vi) providing a bond.
- (f) In September and November 2005, Avantel Infraestructura filed before the Federal Court of Tax and Administrative Justice a lawsuit claiming the lack of answer to a petition previously filed by Avantel Infraestructura requesting confirmation of a criterion. This petition was based on the fact that Avantel is not obligated to pay for some governmental services established under article 232, fraction I, of the Federal Rights Law, with respect to the use of exclusive economic geographic zone in Mexico related to certain landing points in "Playa Niño", region 86, Benito Juarez Itancah Tulum, Carrillo Puerto, and Quintana Roo. The file was turned for study and resolution to the 5th Metropolitan Regional Court of the Federal Court of Tax and Administrative Justice, which is still pending to be admitted.
- (g) The Company leases some equipment and facilities under operating leases. Some of these leases have renewal clauses. Lease expense for 2007, 2006 and 2005 was Ps. 457,457, Ps. 397,591 and Ps. 374,245, respectively.

The annual payments under these leases as of December 31, 2007 are as follows:

		Contracts in:	
		Pesos	Dollars
		(thousands)	(thousands)
2008	Ps.	150,868	\$ 9,352
2009		136,816	7,658
2010		106,682	6,214
2011		84,823	5,637
2012		65,974	5,039
Thereafter		338,001	14,761
	Ps.	<u>883,164</u>	<u>\$ 48,661</u>

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- (h) As of December 31, 2007, the Company has placed purchase orders which are pending delivery from suppliers for approximately Ps. 1,334,617.
- (i) In connection to one of the contracts that Avantel signed with Telmex on October 2006, Avantel should issue a letter of credit in case of change of control in Avantel, situation that occurred during the month of November, at the moment that Axtel acquired the shares from Tel Holding and Banamex. The amount of this instrument is U.S. \$60 million. Axtel is a guarantor of this instrument with Banamex, which issued the letter of credit.

(23) Recently issued accounting standards

The CINIF has issued the following FRS, effective for years beginning after December 31, 2007, and which do not provide for earlier application.

- (a) **FRS B-10 “Effects of inflation”**- FRS B-10 supersedes Bulletin B-10 and its five amendments, as well as the related circulars and INIF (Interpretation of Financial Reporting Standards) 2. The principal considerations established by this FRS are: (i) the change in the value of the Investment Unit (UDI) may be used for determining the inflation for a given period; (ii) the election to use inventory replacement costs as well as specific indexation for fixed assets, is eliminated; (iii) an entity is only required to recognize the effects of inflation when operating in an inflationary economic environment (accumulated inflation equal to or higher than 26% in the most recent three-year period); and (iv) the accounts of Gain or Loss from Holding Non-monetary Assets (RETANM - Spanish abbreviation), Monetary Position Gains or Losses (REPOMO - Spanish abbreviation), and Deficit/Excess in Equity Restatement, will be reclassified to retained earnings, when the unrealized portion is not identified.

Management is still evaluating the impact of this FRS.

- (b) **FRS D-3 “Employee benefits”**- FRS supersedes Bulletin D-3, the portion applicable to Employee Statutory Profit Sharing (ESPS) of Bulletin D-4 and INIF (Interpretation of Financial Reporting Standards) 4. The principal considerations established by this FRS are: (i) a maximum of five years is established for amortizing unrecognized/unamortized items, and the option is provided for immediate recognition of actuarial gains or losses in results of operations; (ii) the recognition of an additional liability and related intangible asset and any related item as a separate element of stockholders' equity, is eliminated; (iii) severance benefits are to be recognized directly in results of operations; and (iv) ESPS, including deferred ESPS, is to be presented in the statement of income as ordinary operations. Furthermore, FRS D-3 establishes that the asset and liability method required by FRS D-4 should be used for determining deferred ESPS, stating that any effects arising from the change are to be recognized in retained earnings, with no restatement of prior years' financial statements.

Management estimates that the initial effects of this new FRS will not be material.

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- (c) **FRS D-4 “Tax on earnings”**- FRS supersedes Bulletin D-4 and Circulars 53 and 54. The principal considerations established by this FRS are: (i) the balance of the cumulative IT effects resulting from the initial adoption of Bulletin D-4 in 2000 is reclassified to retained earnings; (ii) AT is recognized as a tax credit (benefit), rather than as a tax prepayment; and (iii) the accounting treatment of ESPS incurred and deferred is transferred to FRS D-3, as mentioned in paragraph (b) above.

Management estimates that the initial effects of this new FRS will not be material.

- (d) **FRS B-2 “Statement of cash flows”**- FRS supersedes Bulletin B-12 and paragraph 33 of Bulletin B-16. The principal considerations established by this FRS are: (i) the statement of cash flows replaces the statement of changes in financial position; (ii) cash inflows and cash outflows are reported in nominal currency units i.e. the effects of inflation are not included; (iii) two alternative preparation methods (direct and indirect) are established, without stating preference for either method. Furthermore, cash flows from operating activities are to be reported first, followed by cash flows from investing activities and lastly cash flows from financing activities; (iv) captions of principal items are to be reported gross; and (v) disclosure of the composition of those items considered cash equivalents is required.

(24) Subsequent event

- a) On April 23, 2008, Company’s shareholders approved a shares buy-back program for up to Ps. 440 million.
- b) Regarding the legal dispute against Global Towers Communications Mexico S. de R.L. de C.V. mentioned in note 22(a), on April 1, 2008, the trial court ruled against us ordering Axtel to return the deposit and applicable interests. The Company will appeal the trial court’s order before the Superior Court of Appeal.

(25) Differences between Mexican and United States accounting principles

The consolidated financial statements of the Company are prepared according to Financial Reporting Standards in Mexico (Mexican GAAP), which differ in certain significant respects from those, applicable in the United States of America (U.S. GAAP).

The consolidated financial statements under Mexican GAAP include the effects of inflation provided for by Bulletin B-10, whereas the financial statements prepared under U.S. GAAP are presented on a historical cost basis. The following reconciliation does not eliminate the inflation adjustments for Mexican GAAP, since they represent an integral measurement of the effects of the changes in the price levels in the Mexican economy and, as such, are considered a more meaningful presentation than the financial reports based on historic costs for book purposes for Mexico and the United States of America.

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The main differences between Mexican GAAP and U.S. GAAP and their effect on consolidated net income and stockholders' equity as of December 31, 2007, 2006 and 2005 is presented below, with an explanation of the adjustments.

	Year ended December 31,		
	2007	2006	2005
Net income reported under Mexican GAAP Ps			
.	490,996	222,412	307,080
U.S. GAAP adjustments			
1. Deferred income taxes (see 24a)	741,404	1,912	226,971
2. Amortization of start-up cost (see 24c)	47,694	46,745	44,684
3. Start-up costs of the year (see 24c).....	-	(13,991)	(11,049)
4. Allowance for post retirement benefits (see 24d)....	25,391	(5,875)	6,101
5. Revenue recognition (see 24b)	(2,292)	(29,103)	(35,447)
6. Capitalized interest (see 24e).....	(11,540)	(9,548)	(882)
7. Additional depreciation (see 24 h)	(171,152)	-	-
Total U.S. GAAP adjustments.....	629,505	(9,860)	230,378
Net income under U.S. GAAP Ps			
.	1,120,501	212,552	537,458
	Year ended December 31,		
	2007	2006	
Total stockholders' equity reported under Mexican GAAP Ps.	8,750,346	7,884,322	
U.S. GAAP adjustments			
1. Deferred income taxes (see 24a)	832,023	93,956	
2. Start up costs (see 24c)	(111,897)	(159,591)	
3. Revenue recognition (see 24b)	(159,933)	(157,641)	
4. Allowance for post retirement benefits (see 24d)....	1,793	(35,516)	
5. Capitalized interest (see 24e).....	5,639	17,179	
6. SAB 108 adjustment (see 24f).....	109,874	109,874	
7. Additional depreciation expense (see 24 h).....	(171,151)	-	
Total U.S. GAAP adjustments.....	506,348	(131,739)	
Total stockholders' equity under U.S. GAAP Ps.	9,256,694	7,752,583	

The term "SFAS" as used in this document refers to Statement of Financial Accounting Standards.

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(a) *Deferred income taxes (IT)*

For Mexican GAAP, deferred IT are accounted for under the asset and liability method.

For U.S. GAAP purposes, the Company accounts for IT under SFAS 109 “*Accounting for Income Taxes*,” which uses the asset and liability method to account for deferred tax assets and liabilities. Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences of the differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and the tax loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax laws and rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The deferred tax effect of a change in the tax rate is recognized in the results of operations of the period in which the change is enacted. The amount of deferred income taxes charged or credited to the operations in each period, for U.S. GAAP purposes, is based on the difference between the beginning and ending balances of the deferred tax assets and liabilities for each period, expressed in nominal pesos.

All of the Company’s pretax income and reported income tax expense is derived from domestic operations. The income tax (expense) benefit attributable to the income before IT under U.S. GAAP differed from the amount computed by applying the tax rate of 28% in 2007, 29% in 2006 and 30% in 2005 to pretax income, as a result of the items mentioned below:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Computed “expected” income tax (expense)	Ps. (220,069)	(94,696)	(143,510)
(Increase) decrease in income tax expense resulting from:			
Effects of inflation, net	21,431	(7,878)	(1,867)
Change in valuation allowance	567,678	2,649	229,264
Deferred employee’s profit sharing	3,806	-	-
Adjustments to deferred tax assets and liabilities for enacted changes in tax rates	-	12,055	6,479
Accelerated tax depreciation effects	(43,550)	(37,692)	-
(Non-deductible expenses) non-taxable income	(5,757)	5,530	(25,807)
Other	<u>9,572</u>	<u>4,393</u>	<u>(5,469)</u>
Income tax benefit (expense)	Ps. <u>333,111</u>	<u>(115,639)</u>	<u>59,090</u>

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The rollforward for the net deferred tax asset under U.S. GAAP for the years ended December 31, 2007 and 2006 is presented below:

		<u>2007</u>	<u>2006</u>
Balance at the beginning of the year	Ps.	(469,011)	107,195
Deferred IT benefit (expense)		457,023	(110,745)
Deferred IT effects from Avantel's acquisition			
		851,620	(456,920)
Stockholders' equity			
Post retirement benefits		(3,462)	3,462
Fair value of derivative financial instruments		<u>4,586</u>	<u>(11,903)</u>
Balance at the end of the year	Ps.	<u>840,756</u>	<u>(469,011)</u>

The tax effects of temporary differences that give rise to significant portions of deferred tax assets and deferred tax liabilities as of December 31, 2007 and 2006 under U.S. GAAP are presented below:

		<u>2007</u>	<u>2006</u>
Deferred tax assets:			
Net operating loss carryforwards	Ps.	968,090	1,426,521
Allowance for doubtful accounts		126,117	84,496
Accrued liabilities		412,699	382,772
Premium on bond issuance.....		10,179	12,719
Fair value of derivative instruments.....		17,090	12,504
Recoverable AT.....		<u>418,851</u>	<u>332,540</u>
Total gross deferred tax assets		1,953,026	2,251,552
Less valuation allowance		<u>530,355</u>	<u>1,406,881</u>
Net deferred tax assets		<u>1,422,671</u>	<u>844,671</u>
Deferred tax liabilities:			
Property, systems and equipment		410,067	796,402
Telephone concession rights		171,848	232,207
Intangible and other assets		<u>-</u>	<u>285,073</u>
Total gross deferred tax liabilities.....		<u>581,915</u>	<u>1,313,682</u>
Net deferred tax asset (liability) under U.S. GAAP		840,756	(469,011)
Effects from Avantel acquisition.....		<u>927,356</u>	<u>1,183,844</u>

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Less net deferred tax assets recognized under Mexican GAAP	936,089	620,877
U.S. GAAP adjustment to stockholders' equity Ps.	<u>832,023</u>	<u>93,956</u>

Balance sheet classification under US GAAP is as follows:

	2007	2006
Deferred tax assets – current	Ps. 541,150	275,122
Deferred tax assets – long – term	299,606	-
Deferred tax liabilities – long – term	-	(744,133)
Net deferred tax asset (liability) under U.S. GAAP	Ps. <u>840,756</u>	<u>(469,011)</u>

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In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax-planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes it is more likely than not that the Company will realize the benefits of these deductible differences, net of the existing valuation allowances as of December 31, 2007. The amount of the deferred tax asset considered realizable could change if estimates of future taxable income during the carryforward period are changed.

During 2007, the Company made a release of the valuation allowance previously recognized at the Avantel acquisition date in the amount of Ps. 1,219,967. In accordance with SFAS 109, the recognized tax benefit in the reduction of the valuation allowance after the acquisition date was allocated to reduce the intangibles related to that acquisition amounting to Ps. 765,036, less deferred tax effects of Ps. 214,210. The remaining portion amounting to Ps. 669,141 was recorded as a reduction of the income tax expense.

The Company adopted the provisions of FIN 48 on January 1, 2007, and there was no material effect on the consolidated financial statements. As a result, the Company did not record any cumulative effect adjustment related to adopting FIN 48.

As of January 1, 2007, and for the 12-month period ended December 31, 2007, the Company did not have any material unrecognized tax benefits and thus, no interest and penalties related to unrecognized tax benefits were recognized. The Company did not record interest and penalties related to unrecognized tax benefits in the consolidated statements of operations. In addition, the Company does not expect that the amount of unrecognized tax benefits will change significantly within the next 12 months.

The Company and its subsidiaries file standalone income tax returns in Mexico only. With a few exceptions, the Mexican income tax returns of the Company and its subsidiaries are open to examination by the relevant local tax authorities for the tax years beginning in 2002.

(b) *Revenue recognition*

On December 17, 2003, the SEC issued Staff Accounting Bulletin No. 104, "Revenue Recognition in Financial Statements" (SAB 104). This bulletin summarizes the point of view of the SEC in the recognition of revenues in the financial statements according to U.S. GAAP. The SEC concluded that only when all the following conditions are met is revenue recognition appropriate:

- a) there is persuasive evidence of an agreement;
- b) the delivery was made or the services rendered;
- c) the sales price to the purchaser is fixed or determinable; and
- d) collection is reasonable assured.

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SAB 104, specifically in Topic 13A, discusses the situation of recognizing as revenue certain non-refundable up front fees. SAB 104 provides that the seller should not recognize non-refundable charges generated in certain transactions when there is continuous involvement by the vendor.

One of the examples provided by SAB 104 is activation revenues from telecommunication services. The SAB concludes that unless the charge for the activation service is an exchange for products delivered or services rendered that represent the culmination of a separate revenue-generating process, the deferral method of revenue recognition is appropriate.

Based on the provisions and interpretations of SAB 104, for purposes of the U.S. GAAP reconciliation, the Company has deferred the activation revenues over a three-year period starting in the month such charge is originated. This period was determined based on Company's experience with customer retention. The net effect of the deferral and amortization of activation revenues is presented in the U.S. GAAP reconciliation.

(c) *Start-up costs*

In April 1998, the AICPA issued Statement of Position 98-5, "Report of Start-up Costs" (SOP 98-5), which requires start-up costs, including organization costs, to be expensed as incurred. SOP 98-5 is effective, except for certain investment companies, for fiscal years beginning after December 15, 1998. Under Mexican GAAP, these costs were recognized when incurred as a deferred asset and amortized over a period of 10 years. The Company has reversed the amortization expense of Ps. 47,694, Ps. 46,745 and Ps. 44,684 in 2007, 2006 and 2005, as shown in the U.S. GAAP reconciliation, and has reduced stockholders' equity by Ps. 111,897 and Ps. 159,591 to write-off the unamortized balance at each year end. For U.S. GAAP purposes during 2006 and 2005, the Company expensed Ps. 13,991 and Ps. 11,049, respectively of start-up costs capitalized in those periods under Mex GAAP.

(d) *Allowance for post retirement benefits*

For the years ended December 31, 2004 and before, under Mexican GAAP (Bulletin D-3), severance payments were recognized in earnings in the period in which they were paid, unless such payments were used by an entity as a substitution of pension benefits, in which case, they were considered as a pension plan. Starting January 1, 2005, the new Bulletin D-3 replaces the issue of unforeseen payments with the one relating to "Payments Upon Terminations of the Labor Relationship" and establishes certain valuation and disclosure requirements for those payments for reasons other than restructuring, which are the same as those for pension and seniority premium payments. Under U.S. GAAP, post-employment benefits for former or inactive employees, excluding retirement benefits, are accounted for under the provisions of SFAS 112 and SFAS 158, which requires recognition of certain benefits, including severance, over an employee's service life. For the years ended December 31, 2007, 2006 and 2005 the Company recorded a (decrease) increase in net income of Ps. 25,391, Ps. (5,875) and Ps. 6,101, respectively; and for 2006 the Company cancelled a deferred charge of Ps. 17,071, as recorded under Mexican GAAP. The US GAAP liability amounts to Ps. 44,608 and Ps. 65,740 as of December 31, 2007 and 2006, respectively.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Thousands pesos of constant purchasing power as of December 31, 2007)

Effective December 31, 2006, the Company adopted the recognition and disclosure provisions of FASB Statement No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans* (SFAS 158). SFAS 158 requires companies to recognize the funded status of defined benefit pension and other postretirement plans as a net asset or liability and to recognize changes in that funded status in the year in which the changes occur through other comprehensive income to the extent those changes are not included in the net periodic cost. The funded status reported on the balance sheet as of December 31, 2007 and 2006 under SFAS 158 was measured as the difference between the fair value of plan assets and the benefit obligation on a plan-by-plan basis. The Company believes that the assumptions utilized in recording its obligations under its plans are reasonable based on its experience and market conditions. The incremental effect of applying SFAS 158 on the Company's financial position as of December 31, 2007 for items not yet recognized as a component of net periodic cost that were recognized in accumulated other comprehensive income was as follows:

		Before Application of SFAS 158	Adjustments	After Application of SFAS 158
Severance, seniority premiums and other post retirements benefits long term portion	Ps.	47,257	(2,649)	44,608
Deferred income taxes assets (noncurrent)		(13,232)	742	(12,490)
Total liabilities	Ps.	<u>34,025</u>	<u>(1,907)</u>	<u>32,118</u>

(e) Capitalized interest

Under Mexican GAAP, the Company capitalizes interest on property, systems and equipment under construction. The amount of financing cost to be capitalized is comprehensively measured in order to include properly the effects of inflation. Therefore, the amount capitalized includes: (i) the interest cost of the debt incurred, plus (ii) any foreign currency fluctuations that result from the related debt, and less (iii) the monetary position gain recognized on the related debt. Under U.S. GAAP, only interest is considered an additional cost of constructed assets to be capitalized and depreciated over the lives of the related assets.

The U.S. GAAP reconciliation removes the foreign currency gain or loss and the monetary position gain capitalized for Mexican GAAP derived from borrowings denominated in foreign currency.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Thousands pesos of constant purchasing power as of December 31, 2007)

(f) Staff Accounting Bulletin 108

In September 2006, the SEC issued Staff Accounting Bulletin No. 108 (“SAB 108”) “*Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements*,” that provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. There are two widely recognized methods for quantifying the effects of financial statement misstatements: the “rollover” or income statement method and the “iron curtain” or balance sheet method. The SEC staff believes that registrants should quantify errors using both a balance sheet and an income statement approach (“dual method”) and evaluate whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. SAB 108 permits companies to apply its provisions initially by either (i) restating prior financial statements as if the provisions had always been applied or (ii) recording the cumulative effect of initially applying SAB 108 as adjustments to the carrying value of assets and liabilities as of the beginning of 2006 with an offsetting adjustment recorded to the opening balance of stockholders’ equity. Upon adoption of SAB 108, we recorded a one-time cumulative effect adjustment to increase the beginning-of-year balance of stockholders’ equity of Ps. 109,874 for prior year misstatements that previously had been considered immaterial. The Company believes its prior period assessments of uncorrected misstatements and the conclusions reached regarding its quantitative and qualitative assessments of materiality of such items, both individually and in the aggregate, were appropriate. In accordance with SAB 108, the Company has adjusted its opening stockholders’ equity for 2006 for the items described below:

Capitalized Interest: The Company adjusted its beginning stockholders’ equity for 2006 related to recording interest capitalized taken directly to interest expense rather than being shown as an increase in property, systems and equipment. It was determined that the Company had improperly excluded approximately Ps. 186,954 which should have been shown as an increase in property, systems and equipment.

Capitalized Costs: The Company adjusted its beginning stockholders’ equity for 2006 related to historical capitalization of certain costs considered immaterial under the previously established policy of capitalizing costs. It was determined that the Company had improperly recorded an increase in property systems and equipment for Ps. (77,078).

The cumulative effects of the items noted above for 2006 beginning balances are presented below:

Description		Property, Systems and Equipment	Deferred Taxes	Stockholders’ Equity
Property, systems and equipment	Ps.	164,036	-	164,036
Deferred taxes		-	(54,162)	(54,162)
Total	Ps.	<u>164,036</u>	<u>(54,162)</u>	<u>109,874</u>

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Thousands pesos of constant purchasing power as of December 31, 2007)

(g) Supplemental cash flow information under U.S. GAAP

Under Mexican GAAP, statements of changes in financial position identify the sources and uses of resources based on the differences between beginning and ending consolidated financial statement balances in constant pesos. Monetary position results and unrealized foreign exchange results are treated as cash items in the determination of resources provided by operations. Under U.S. GAAP (SFAS 95), statements of cash flows present only cash items and exclude non-cash items. SFAS 95 does not provide guidance with respect to inflation-adjusted financial statements. The differences between Mexican GAAP and U.S. GAAP in the amounts reported are mainly due to: (i) elimination of inflationary effects of monetary assets and liabilities from financing and investing activities against the corresponding monetary position result in operating activities, (ii) elimination of foreign exchange results from financing and investing activities against the corresponding unrealized foreign exchange result included in operating activities, and (iii) the recognition in operating, financing and investing activities of the U.S. GAAP adjustments.

The following table summarizes the cash flow items as required under SFAS 95 provided by operating, financing and investing activities, giving effect to the U.S. GAAP adjustments, excluding the effects of inflation required by Bulletin B-10. The following information is presented in thousands of pesos on a historical peso basis and is not presented in pesos of constant purchasing power:

		Years ended December 31,		
		2007	2006	2005
Operating activities:				
Net income	Ps.	1,120,501	204,851	497,809
Adjustments to reconcile net income to cash provided by operating activities:				
Depreciation		2,507,636	1,365,621	1,018,138
Amortization		343,419	96,398	71,523
Allowance for severance and seniority premiums		(12,779)	17,684	(4,117)
Income tax and employees' profit sharing expense (benefit)		(443,429)	112,567	(54,731)
Bad debt expense		194,108	119,563	80,274
Monetary position gain		(279,985)	(15,524)	(57,846)
Exchange (gain) loss		(19,942)	1,067	(103,857)
Equity in results of associated company		(1,430)	(1,592)	-
Change in accounts receivable		(416,058)	(1,066,703)	(225,946)
Changes in inventory		(68,553)	(37,970)	(3,116)
Changes in other assets		101,791	(918,191)	16,980
Changes in accounts payable		135,840	1,275,156	(141,724)
Changes in other accounts payable		(27,915)	928,348	26,437
Change in deferred revenues		(59,286)	294,156	-
Changes in allowance for severance and seniority premiums		(14,175)	48,603	2,743
Net cash provided by operating activities		<u>3,059,743</u>	<u>2,424,034</u>	<u>1,122,567</u>

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

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Financing activities:

Proceeds from sale of common stock	374,730	-	1,045,093
Costs incurred in sale of common stock	-	(12,764)	-
Proceeds from loans	3,102,308	6,521,438	996,530
Payments of loans	(3,527,584)	(1,209,831)	(251,696)
Deferred financing costs	-	(86,572)	-
Restricted cash	-	34,479	(34,479)
Notes issuance costs	-	-	(18,483)
Other accounts payable	<u>3,310</u>	<u>(47,360)</u>	<u>34,921</u>
Net cash (used in) provided by financing activities	<u>(47,236)</u>	<u>5,199,390</u>	<u>1,771,886</u>

Investing activities:

Acquisition of property, systems and equipment	(2,534,481)	(2,389,380)	(1,548,316)
Acquisition of Avantel, net of cash acquired	-	(5,133,226)	-
Intangible assets	-	(724,834)	-
Investment in shares of associated company	-	(12,023)	-
Other assets	<u>(82,016)</u>	<u>(77,139)</u>	<u>(9,493)</u>
Net cash used in investing activities	<u>(2,616,497)</u>	<u>(8,336,602)</u>	<u>(1,557,809)</u>
Net increase (decrease) in cash and cash equivalents	396,010	(713,178)	1,336,644
Cash and cash equivalents at beginning of year	<u>1,177,867</u>	<u>1,891,045</u>	<u>554,401</u>
Cash and cash equivalents at end of year	Ps. <u>1,573,877</u>	<u>1,177,867</u>	<u>1,891,045</u>

Non-cash operating and investing activities:

For the years ended December 31, 2007, 2006 and 2005 the Company has Ps. 99,275, Ps. 69,775 and Ps. 95,375 in accounts payable for acquisition of property, systems and equipment, respectively. Additionally, the Company adopted the guidelines of SFAS 158. The net effects of the recognition of the statement amounted to Ps. 8,581 in allowance for post retirement benefits and accumulated other comprehensive income.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Thousands pesos of constant purchasing power as of December 31, 2007)

Non-cash financing and investing activities:

Net cash flows provided from operating activities reflect cash payments for interest and income taxes as follows:

		Years Ended December 31,		
		2007	2006	2005
Interest paid	Ps.	1,190,221	252,129	314,181
Income taxes paid		101,305	3,598	2,170

(h) Condensed financial information under U.S. GAAP

The following table presents consolidated condensed statements of operations for the years ended December 31, 2007, 2006 and 2005, prepared under U.S. GAAP, and includes all differences described in note 24 as required for purposes of U.S. GAAP:

		Years Ended December 31,		
		2007	2006	2005
Statements of operations				
Revenues	Ps.	12,182,607	6,641,601	5,323,973
Operating income		1,207,064	682,781	645,982
Comprehensive financing result		(420,666)	(320,473)	(175,349)
Other (expenses) income, net		(438)	(35,770)	7,735
Income before taxes and equity in income of associated company		785,960	326,538	478,368
Income tax benefit (expense) benefit		333,111	(115,639)	59,090
Equity in income of associated company		1,430	1,653	-
Consolidated net income	Ps.	1,120,501	212,552	537,458

The following table presents consolidated condensed balance sheets as of December 31, 2007 and 2006, prepared under U.S. GAAP, including all differences and reclassification pertaining to the presentation of deferred income taxes, as compared to Mexican GAAP described in this note 24:

		As of December 31,	
		2007	2006
Balance sheets			
Current assets	Ps.	4,264,070	3,282,299
Property, systems and equipment		14,996,050	15,075,296
Other assets		1,235,045	2,049,740
Total assets	Ps.	20,495,165	20,407,335
Current liabilities	Ps.	3,328,421	3,355,751
Long-term debt		7,484,955	8,294,282
Other non-current liabilities		425,095	1,004,719
Total liabilities		11,238,471	12,654,752
Stockholders' equity		9,256,694	7,752,583
Total liabilities and stockholders' equity	Ps.	20,495,165	20,407,335

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Thousands pesos of constant purchasing power as of December 31, 2007)

In connection with the preliminary purchase price allocation to the assets and liabilities acquired in the Avantel acquisition, certain differences occurred between Mexican reporting standards and U.S. GAAP. For U.S. GAAP purposes goodwill which is included as part of other assets, amounting to Ps. 168,525 was initially recognized as a result of the acquisition of Avantel in accordance with FASB 141 “*Business Combinations*”. During the year the adjustments recorded to the preliminary purchase price allocation to the assets and liabilities were as follows:

		Preliminary Value	Adjustments	Definitive Value
<u>Balance Sheet:</u>				
Current assets	Ps.	1,242,121	-	1,242,121
Property, systems and equipments, net		7,426,445	216,293	7,642,738
Intangible assets		939,899	(174,863)	765,036
Goodwill		168,525	(168,525)	-
Others		84,604	=	84,604
		<u>9,861,594</u>	<u>(127,095)</u>	<u>9,734,499</u>
Total of assets acquired		9,861,594	(127,095)	9,734,499
Current liabilities		2,455,832	(109,586)	2,346,246
Deferred income tax		381,715		381,715
Long term liabilities		867,201	(17,509)	849,692
		<u>3,704,748</u>	<u>(127,095)</u>	<u>3,577,653</u>
Total of liabilities assumed		3,704,748	(127,095)	3,577,653
Net assets acquired	Ps.	<u>6,156,846</u>		<u>6,156,846</u>

The main adjustments are detailed as follows:

- Property, systems and equipment: The additional adjustments during the period were related with the final appraisal realized by independent experts, cancellation of systems that will not be used anymore and will be replaced by systems of Axtel and the effects of the of negative goodwill. Because the value of property, systems and equipment under US GAAP is higher than under Mexican GAAP and additional depreciation expense amounting to Ps. 171,151 was recorded.
- Intangible assets: The additional adjustments during the period were related with the final appraisal realized by independent experts and the effects of the negative goodwill.
- Current liabilities: These adjustments correspond to the elimination of the accrual created in connection to the early termination of links leased by Avantel. The terminated contracts did not have any cost associated.
- Long-term liabilities: This adjustment corresponds to the cancellation of the pension plan as mentioned in note 18.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

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(i) Fair value of financial instruments

The carrying amount of cash, trade accounts receivable, other accounts receivable, trade accounts payable, other accounts payable and accrued expenses and short-term debt, approximates fair value because of the short-term maturity of these financial assets and liabilities.

The carrying value of the Company's long-term debt and the related fair value based on quoted market prices for the same or similar instruments or on current rates offered to the Company for debt of the same remaining maturities (or determined by discounting future cash flows using borrowing rates currently available to the Company) as of December 31, 2013 is summarized as follows:

	Carrying amount	Estimated fair value
Long-term debt.....	654,744	623,961

(j) Segment information

The Company believes that it operates in one business segment. Management does view the business as consisting of two revenues streams (Mass market and Business Market); however it is not possible to attribute direct or indirect costs to the individual streams other than selling expenses.

(k) Recently Issued Accounting Standards

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities – including an amendment of FASB Statement No. 115 (Statement 159). Statement 159 gives the Company the irrevocable option to carry most financial assets and liabilities at fair value that are not currently required to be measured at fair value. If the fair value option is elected, changes in fair value would be recorded in earnings at each subsequent reporting date. SFAS 159 is effective for the Company's 2008 fiscal year. The Company does not expect that this will have a material impact in the financial statements.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements." SFAS No. 157 clarifies the principle that fair value should be based on the assumptions that market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. Under SFAS No. 157, fair value measurements would be separately disclosed by level within the fair value hierarchy. In February 2008, the FASB approved FASB Staff Position FAS 157-2 ("FSP 157-2") that permits companies to partially defer the effective date of SFAS No. 157 for one year for nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. FSP 157-2 did not permit companies to defer recognition and disclosure requirements for financial assets and financial liabilities or for nonfinancial assets and nonfinancial liabilities that are remeasured at least annually. SFAS No. 157 is effective for financial assets and financial liabilities and for nonfinancial assets and nonfinancial liabilities that are remeasured at least annually for the Company's fiscal year beginning January 1, 2008. The Company will defer adoption of SFAS No. 157 for one year for nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. The Company does not expect that this will have a material impact in the financial statements.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

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In December 2007, the FASB issued SFAS No. 141 (revised 2007), "Business Combinations" ("SFAS No. 141(R)"). SFAS No. 141(R) expands the definition of a business combination and requires the fair value of the purchase price of an acquisition, including the issuance of equity securities, to be determined on the acquisition date. SFAS No. 141(R) also requires that all assets, liabilities, contingent considerations and contingencies of an acquired business be recorded at fair value at the acquisition date. In addition, SFAS No. 141(R) requires that acquisition costs generally be expensed as incurred, restructuring costs generally be expensed in periods subsequent to the acquisition date and changes in accounting for deferred tax asset valuation allowances and acquired income tax uncertainties after the measurement period impact income tax expense. SFAS No. 141(R) is effective for the Company's fiscal year beginning December 15, 2008 on a prospective basis for all business combinations for which the acquisition date is on or after the effective date of SFAS No. 141(R), with the exception of the accounting for adjustments to income tax-related amounts, which is applied to acquisitions that closed prior to the effective date of SFAS No. 141(R). The Company is evaluating the effect the implementation of SFAS No. 141(R) will have on the consolidated financial statements.

In December 2007, the FASB issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements, an Amendment of ARB No. 51." SFAS No. 160 changes the accounting and reporting for minority interests such that minority interests will be recharacterized as noncontrolling interests and will be required to be reported as a component of equity, and requires that purchases or sales of equity interests that do not result in a change in control be accounted for as equity transactions and, upon a loss of control, requires the interest sold, as well as any interest retained, to be recorded at fair value with any gain or loss recognized in earnings. SFAS No. 160 is effective for the Company's fiscal year beginning December 15, 2008 with early adoption prohibited. The Company is evaluating the effect the implementation of SFAS No. 160 will have on the consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities." SFAS No. 161 amends and expands the disclosure requirements of SFAS No. 133 for derivative instruments and hedging activities. SFAS No. 161 is effective for the Company's fiscal year beginning November 15, 2008 with early adoption permitted. SFAS No. 161 does not impact the consolidated financial statements and the Company is evaluating the effect the implementation will have on the Notes to Consolidated Financial Statements.

In September 2006, the FASB's Emerging Issues Task Force reached a consensus on Issue No. 06-4, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements (EITF 06-4). EITF 06-4 provides guidance on the accounting for arrangements in which an employer owns and controls the insurance policy and has agreed to share a portion of the cash surrender value and/or death benefit with the employee. This guidance requires an employer to record a postretirement benefit, in accordance with FASB Statement No. 106, Employers' Accounting for Postretirement Benefits Other Than Pensions" or APB Opinion No. 12, "Omnibus Opinion-1967, if there is an agreement by the employer to share a portion of the proceeds of a life insurance policy with the employee during the postretirement period. This guidance is effective for reporting periods beginning after December 15, 2007. The Company is in the process of assessing the impact of adopting EITF 06-4 on its results of operations and financial position; however, the company currently expects that additional liabilities may be required to be recognized upon implementation of the consensus based on the current terms of certain life insurance arrangements with executive officers of the Company.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

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(I) *Guaranteed debt*

On December 16, 2003, the Company completed an offering of senior unsecured notes, for a value of U.S. \$175 million maturing on December 15, 2013. In addition, during January 2005, the Company re-opened its bond issuance program, issuing U.S. \$75 million under the 2003 indenture. Interest on the notes are payable semiannually at annual rate of 11%, since June 15, 2004.

Each of the Company's consolidated subsidiaries, Instalaciones y Contrataciones, S.A. de C.V. (Instalaciones), Impulsora e Inmobiliaria Regional, S.A. de C.V. (Impulsora) and Servicios Axtel, S.A. de C.V. (Servicios), are guaranteeing the notes with unconditional guaranties that are unsecured. Each of the subsidiaries guarantors are 99.99% owned by Axtel, S.A. de C.V. All guarantees are full and unconditional and are joint and several.

AXTEL is eligible, under Adopting Release (nos. 33-7878 and 34-43124) and a no-action request letter, for presenting the condensed consolidating financial information of Impulsora, Instalaciones and Servicios in this note in accordance with Rule 3-10 (f) of Regulation S-X. Impulsora, Instalaciones and Servicios have total capital stock outstanding of 1,500,000, 9,246,154 and 51,050,000 common shares. Axtel directly owns all but one share of each of Impulsora, Instalaciones and Servicios. The ownership of the remaining share by someone other than Axtel is a requirement of Mexican law.

For the purpose of the accompanying condensed consolidating balance sheets, income statements and changes in financial position under Mexican GAAP, the first column "AXTEL" corresponds to the parent company issuer. The second column, "Combined Guarantors", represents the combined amounts of Instalaciones, Impulsora and Servicios, after adjustments and eliminations relating to their combination. The third column "Combined non-guarantors" represents the combined amounts of AXTEL's non-guarantors subsidiaries, after adjustments and eliminations relating to their combination. The fourth column, "Adjustments and Eliminations", includes all amounts resulting from the consolidation of AXTEL, the guarantors and the non-guarantors subsidiaries. The fifth column, "AXTEL Consolidated", represents the Company's consolidated amounts as reported in the audited consolidated financial statements. Additionally, all amounts presented under the line item "Investments in subsidiaries" for both the balance sheet and the income statement are accounted for by the equity method.

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Thousands pesos of constant purchasing power as of December 31, 2007)

The condensed consolidating financial information is as follows:

Condensed consolidating balance sheets:

			Combined	Combined	Adjustments and	AXTEL
As of December 31, 2007		AXTEL	Guarantors	Non-guarantors	Eliminations	Consolidated
Current assets	Ps.	2,621,784	355,949	1,876,572	(1,131,385)	3,722,920
Property, systems and equipment, net		12,759,605	8,158	912,559	(451)	13,679,871
Concession rights, pre-operating expenses and deferred taxes		1,065,811	53,481	1,092,327	(91,249)	2,120,370
Investment in subsidiaries		1,279,191	-	15,249	(1,279,191)	15,249
Other non-current assets and long-term receivable		228,231	930	63,106	-	292,267
Total assets	Ps.	17,954,622	418,518	3,959,813	(2,502,276)	19,830,677
Current liabilities	Ps.	2,062,722	336,386	2,060,698	(1,131,385)	3,328,421
Long-term debt		7,069,771	-	415,184	-	7,484,955
Other non-current liabilities		71,783	57,514	203,226	(65,568)	266,955
Total liabilities		9,204,276	393,900	2,679,108	(1,196,953)	11,080,331
Total stockholders equity		8,750,346	24,618	1,280,705	(1,305,323)	8,750,346
Total liabilities and stockholders equity	Ps.	17,954,622	418,518	3,959,813	(2,502,276)	19,830,677
As of December 31, 2006						
Current assets	Ps.	2,742,457	216,933	1,988,110	(1,665,201)	3,282,299
Property, systems and equipment, net		13,214,169	8,900	814,297	(765)	14,036,601
Concession rights, pre-operating expenses and deferred taxes		1,431,989	20,662	1,289,347	(510,942)	2,231,056
Investment in subsidiaries		366,803	-	14,127	(366,803)	14,127
Other non-current assets and long-term receivable		256,493	18,115	55,285	-	329,893
Total assets	Ps.	18,011,911	264,610	4,161,166	(2,543,711)	19,893,976
Current liabilities	Ps.	1,867,927	179,837	2,973,186	(1,665,201)	3,355,749
Long-term debt		7,745,706	-	548,576	-	8,294,282
Other non-current liabilities		513,956	28,571	328,038	(510,942)	359,623
Total liabilities		10,127,589	208,408	3,849,800	(2,176,143)	12,009,654
Total stockholders equity		7,884,322	56,202	311,366	(367,568)	7,884,322
Total liabilities and stockholders equity	Ps.	18,011,911	264,610	4,161,166	(2,543,711)	19,893,976

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

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Condensed consolidating income statements:

For the year ended December 31, 2007		AXTEL	Combined Guarantors	Combined Non-guarantors	Adjustments and Eliminations	AXTEL Consolidated
Telephone services and related revenues	Ps.	7,613,558	2,278,709	5,835,570	(3,537,227)	12,190,610
Cost of revenues and services		(1,919,571)	-	(3,806,717)	1,221,575	(4,504,713)
Selling and administrative expenses		(2,687,835)	(2,257,805)	(971,439)	2,315,652	(3,601,427)
Depreciation and amortization		(2,431,430)	(433)	(261,614)	2,790	(2,690,687)
Operating income		574,722	20,471	795,800	2,790	1,393,783
Comprehensive financing result, net		(445,793)	(2,562)	(53,299)	757	(500,897)
Other (expenses) income, net		(36,000)	(62,668)	247,122	(168,574)	(20,120)
Income tax		(72,984)	13,488	(134,155)	(189,549)	(383,200)
Investment in subsidiaries		471,051	-	1,430	(471,051)	1,430
Net income (loss)	Ps.	490,996	(31,271)	856,898	(825,627)	490,996
For the year ended December 31, 2006						
Telephone services and related revenues	Ps.	6,160,475	1,353,883	689,836	(1,528,482)	6,675,712
Cost of revenues and services		(1,811,343)	-	(361,034)	68,016	(2,104,361)
Selling and administrative expenses		(2,154,854)	(1,361,461)	(204,256)	1,460,466	(2,260,105)
Depreciation and amortization		(1,557,081)	(470)	(2,503)	-	(1,560,054)
Operating income (loss)		637,197	(8,048)	122,043	-	751,192
Comprehensive financing result, net		(281,859)	(2,784)	(96,792)	1,194	(380,241)
Other income, net		(28,564)	3,368	(6,251)	(1,194)	(32,641)
Income tax		(125,984)	2,793	5,641	-	(117,550)
Investment in subsidiaries		21,622	-	1,652	(21,622)	1,652
Net income (loss)	Ps.	222,412	(4,671)	26,293	(21,622)	222,412

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Thousands pesos of constant purchasing power as of December 31, 2007)

For the year ended December 31, 2005		AXTEL	Combined Guarantors	Combined Non-guarantors	Adjustments and Eliminations	AXTEL Consolidated
Telephone services and related revenues	Ps.	5,362,393	1,092,908	-	(1,092,908)	5,362,393
Cost of revenues and services		(1,673,995)	-	-	-	(1,673,995)
Selling and administrative expenses		(1,799,405)	(1,115,352)	-	1,092,908	(1,821,849)
Depreciation and amortization		(1,219,741)	(512)	-	-	(1,220,253)
Operating income (loss)		669,252	(22,956)	-	-	646,296
Comprehensive financing result, net		(178,373)	(2,191)	-	1,494	(179,070)
Other income, net		7,579	1,650	-	(1,494)	7,735
Income tax		(171,422)	3,541	-	-	(167,881)
Investment in subsidiaries		(19,956)	-	-	19,956	-
Net income (loss)	Ps.	<u>307,080</u>	<u>(19,956)</u>	<u>-</u>	<u>19,956</u>	<u>307,080</u>

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Thousands pesos of constant purchasing power as of December 31, 2007)

Condensed consolidating statements of changes in financial position:

			Combined	Combined	Adjustments	
			Guarantors	Non-guarantors	and	AXTEL
For the year ended December 31, 2007		AXTEL			Eliminations	Consolidated
Operating activities:						
Net income (loss)	Ps.	490,996	(31,271)	856,898	(825,627)	490,996
Charges (credits) to operations not requiring (providing) resources		2,033,363	17,286	266,126	681,781	2,998,556
Resources provided by (used in) operations		2,524,359	(13,985)	1,123,024	(143,846)	3,489,552
Net financing from (investment in) operations		(242,211)	(5,710)	(396,531)	381,648	(262,804)
Resources provided by (used in) operating activities		2,282,148	(19,695)	726,493	237,802	3,226,748
Financing activities:						
Increase in common stock		192,280	-	-	-	192,280
Additional paid-in capital		194,540	-	-	-	194,540
Proceeds (payments of) from loans, net		(678,946)	(635)	(133,425)	635	(812,371)
Restricted cash and other accounts payable		106,926	-	-	-	106,926
Resources provided by financing activities		(185,200)	(635)	(133,425)	635	(318,625)
Investing activities:						
Acquisition and construction of property, systems and equipment, net		(2,175,318)	(3)	(102,826)	(207,946)	(2,486,093)
Increase in investment in subsidiaries		-	-	-	-	-
Other assets		(51,252)	17,186	(5,741)	(30,491)	(70,298)
Resources used in investing activities		(2,226,570)	17,183	(108,567)	(238,437)	(2,556,391)
(Decrease) increase in cash and equivalents		(129,622)	(3,147)	484,501	-	351,732
Cash and equivalents at the beginning of the year		912,799	5,054	304,292	-	1,222,145
Cash and equivalents at the end of the year	Ps.	783,177	1,907	788,793	-	1,573,877

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Thousands pesos of constant purchasing power as of December 31, 2007)

For the year ended December 31, 2006		AXTEL	Combined Guarantors	Combined Non- guarantors	Adjustments and Eliminations	AXTEL Consolidated
Operating activities:						
Net income (loss)	Ps.	222,412	(4,671)	26,293	(21,622)	222,412
Charges (credits) to operations not requiring (providing) resources		<u>1,661,446</u>	<u>(95)</u>	<u>(6,223)</u>	<u>23,705</u>	<u>1,678,833</u>
Resources provided by (used in) operations		1,883,858	(4,766)	20,070	2,083	1,901,245
Net financing from (investment in) operations		<u>288,377</u>	<u>(21,400)</u>	<u>(366,427)</u>	<u>(2,553)</u>	<u>630,851</u>
Resources provided by (used in) operating activities		<u>2,172,235</u>	<u>(26,166)</u>	<u>386,497</u>	<u>(470)</u>	<u>2,532,096</u>
Financing activities:						
Increase in common stock		-	24,439	285,075	(309,514)	-
Additional paid-in capital		(9,804)	-	-	-	(9,804)
Proceeds (payments of) from loans, net		4,742,230	(470)	667,696	470	5,409,926
Restricted cash and other accounts payable		<u>48,891</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>48,891</u>
Resources provided by financing activities		<u>4,781,317</u>	<u>23,969</u>	<u>952,771</u>	<u>(309,044)</u>	<u>5,449,013</u>
Investing activities:						
Acquisition and construction of property, systems and equipment, net		(7,037,705)	(24)	(816,800)	-	(7,854,529)
Increase in investment in subsidiaries		(309,514)	-	(12,474)	309,514	(12,474)
Other assets		<u>(731,473)</u>	<u>3,550</u>	<u>(205,701)</u>	<u>-</u>	<u>(933,624)</u>
Resources used in investing activities		<u>(8,078,692)</u>	<u>3,526</u>	<u>(1,034,975)</u>	<u>309,514</u>	<u>(8,800,627)</u>
(Decrease) increase in cash and equivalents		(1,125,140)	1,329	304,293	-	(819,518)
Cash and equivalents at the beginning of the year		<u>2,037,939</u>	<u>3,724</u>	<u>-</u>	<u>-</u>	<u>2,041,663</u>
Cash and equivalents at the end of the year	Ps.	<u>912,799</u>	<u>5,053</u>	<u>304,293</u>	<u>-</u>	<u>1,222,145</u>

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Thousands pesos of constant purchasing power as of December 31, 2007)

For the year ended December 31, 2005		AXTEL	Combined Guarantors	Adjustments and Eliminations	AXTEL Consolidated
Operating activities:					
Net income (loss)	Ps.	307,080	(19,956)	19,956	307,080
Charges (credits) to operations not requiring (providing) resources		1,411,118	5,205	(19,956)	1,396,367
Resources provided by (used in) operations		1,718,198	(14,751)	-	1,703,447
Net investment in operations		(184,236)	5,600	(706)	(179,342)
Resources provided by (used in) operating activities		1,533,962	(9,151)	(706)	1,524,105
Financing activities:					
Increase in common stock		751,832	28,628	(28,628)	751,832
Additional paid-in capital		400,108	-	-	400,108
Payments of loans, net		612,213	(706)	706	612,213
Others		(39,077)	-	-	(39,077)
Resources provided by financing activities		1,725,076	27,922	(27,922)	1,725,076
Investing activities:					
Acquisition and construction of property, systems and equipment, net		(1,767,041)	(51)	-	(1,767,092)
Investment in subsidiaries		(28,628)	-	28,628	-
Other assets		(41,498)	(17,238)	-	(58,736)
Resources used in investing activities		(1,837,167)	(17,289)	28,628	(1,825,828)
(Decrease) increase in cash and equivalents		1,421,871	1,482	-	1,423,353
Cash and equivalents at the beginning of the year		616,068	2,242	-	618,310
Cash and equivalents at the end of the year	Ps.	2,037,939	3,724	-	2,041,663

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Thousands pesos of constant purchasing power as of December 31, 2007)

The tables below present combined balance sheets as of December 31, 2007 and 2006, and income statements and statements of changes in financial position for each of the years in the three-year period ended December 31, 2007 for the Guarantors. Such information presents in separate columns each individual Guarantor, consolidation adjustments and eliminations, and the combined guarantors. All significant related parties' balances and transactions between the Guarantors have been eliminated in the "Combined Guarantors" column.

The amounts presented in the column "Combined Guarantors" are readily comparable with the information of the Guarantors included in the condensed consolidated financial information.

Guarantors' Combined Balance Sheets:

As of December 31, 2007

Assets		Icosa	Inmobiliaria	Servicios Axtel	Adjustments and Eliminations	Combined Guarantors
Cash and cash equivalents	Ps.	513	24	1,370	-	1,907
Related parties receivables		42,882	-	271,742	(4)	314,620
Refundable taxes and other accounts receivable		1,410	1,206	36,806	-	39,422
Total current assets		44,805	1,230	309,918	(4)	355,949
Property, systems and equipment, net		-	8,158	-	-	8,158
Deferred income taxes and employees' profit sharing		3,172	-	50,416	(107)	53,481
Other non-current assets		403	123	404	-	930
Total assets	Ps.	48,380	9,511	360,738	(111)	418,518
Liabilities and Stockholders Equity						
Account payable and accrued liabilities	Ps.	729	-	98,504	-	99,233
Taxes payable		22,602	14	116,005	-	138,621
Related parties payables		-	7,772	4	(4)	7,772
Other accounts payable		4,569	-	86,191	-	90,760
Total current liabilities		27,900	7,786	300,704	(4)	336,386
Deferred income taxes		-	107	-	(107)	-
Other non-current liabilities		6,270	-	51,244	-	57,514
Total liabilities		34,170	7,893	351,948	(111)	393,900
Equity		13,415	1,476	40,998	-	55,889
Net income (loss)		795	142	(32,208)	-	(31,271)
Total stockholders' equity		14,210	1,618	8,790	-	24,618
Total liabilities and stockholders equity	Ps.	48,380	9,511	360,738	(111)	418,518

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Thousands pesos of constant purchasing power as of December 31, 2007)

As of December 31, 2006

Assets		Icosa	Inmobiliaria	Servicios Axtel	Adjustments and Eliminations	Combined Guarantors
Cash and cash equivalents	Ps.	482	8	4,563	-	5,053
Accounts receivable		-	-	-	-	-
Related parties receivables		25,950	-	170,633	-	196,583
Refundable taxes and other accounts receivable		1,360	1,310	12,627	-	15,297
Total current assets		27,792	1,318	187,823	-	216,933
Property, systems and equipment, net		-	8,900	-	-	8,900
Deferred income taxes		1,111	-	19,702	(151)	20,662
Other non-current assets		1,695	128	16,292	-	18,115
Total assets	Ps.	30,598	10,346	223,817	(151)	264,610
Liabilities and Stockholders' Equity						
Account payable and accrued liabilities	Ps.	221	-	32,866	-	33,087
Taxes payable		11,059	-	73,095	-	84,154
Related parties payables		-	8,407	-	-	8,407
Other accounts payable		2,678	-	51,511	-	54,189
Total current liabilities		13,958	8,407	157,472	-	179,837
Deferred income taxes		-	151	-	(151)	-
Other non-current liabilities		3,225	-	25,346	-	28,571
Total liabilities		17,183	8,558	182,818	(151)	208,408
Equity		12,349	1,501	47,023	-	60,873
Net income (loss)		1,066	287	(6,024)	-	(4,671)
Total stockholders' equity		13,415	1,788	40,999	-	56,202
Total liabilities and stockholders equity	Ps.	30,598	10,346	223,817	(151)	264,610

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Thousands pesos of constant purchasing power as of December 31, 2007)

Guarantors' Combined Income Statements:

<u>For the year ended December 31, 2007</u>	<u>Icosa</u>	<u>Inmobiliaria</u>	<u>Servicios Axtel</u>	<u>Adjustments and Eliminations</u>	<u>Combined Guarantors</u>
Rental, installation service and other revenues	Ps. 287,005	2,110	1,989,594	-	2,278,709
Administrative expenses	(279,934)	(500)	(1,977,871)	500	(2,257,805)
Depreciation and amortization	-	(430)	(3)	-	(433)
Operating income	7,071	1,180	11,720	500	20,471
Comprehensive financing result, net	(850)	(915)	(797)	-	(2,562)
Other (expenses) income, net	(4,014)	-	(58,154)	(500)	(62,668)
Income (loss) before income taxes	2,207	265	(47,231)	-	(44,759)
Income taxes	(1,412)	(123)	15,023	-	13,488
Net income (loss)	Ps. <u>795</u>	<u>142</u>	<u>(32,208)</u>	<u>-</u>	<u>(31,271)</u>
<u>For the year ended December 31, 2006</u>					
Rental, installation service and other revenues	Ps. 167,577	2,106	1,184,200	-	1,353,883
Administrative expenses	(165,872)	(519)	(1,195,589)	519	(1,361,461)
Depreciation and amortization	-	(446)	(24)	-	(470)
Operating income (loss)	1,705	1,141	(11,413)	519	(8,048)
Comprehensive financing result, net	(462)	(918)	(1,404)	-	(2,784)
Other (expenses) income, net	(223)	-	4,110	(519)	3,368
Income (loss) before income taxes	1,020	223	(8,707)	-	(7,464)
Income taxes	46	64	2,683	-	2,793
Net income (loss)	Ps. <u>1,066</u>	<u>287</u>	<u>(6,024)</u>	<u>-</u>	<u>(4,671)</u>

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Thousands pesos of constant purchasing power as of December 31, 2007)

<u>For the year ended December 31, 2005</u>	<u>Icosa</u>	<u>Inmobiliaria</u>	<u>Servicios Axtel</u>	<u>Adjustments and Eliminations</u>	<u>Combined Guarantors</u>
Rental, installation service and other revenues	Ps. 116,745	2,112	974,051	-	1,092,908
Administrative expenses	(118,329)	(259)	(997,023)	259	(1,115,352)
Depreciation and amortization	<u>-</u>	<u>(461)</u>	<u>(51)</u>	<u>-</u>	<u>(512)</u>
Operating (loss) income	(1,584)	1,392	(23,023)	259	(22,956)
Comprehensive financing result, net	(236)	(1,244)	(711)	-	(2,191)
Other income, net	<u>19</u>	<u>-</u>	<u>1,890</u>	<u>(259)</u>	<u>1,650</u>
(Loss) income before income taxes	(1,801)	148	(21,844)	-	(23,497)
Income taxes	<u>172</u>	<u>42</u>	<u>3,327</u>	<u>-</u>	<u>3,541</u>
Net (loss) income	Ps. <u>(1,629)</u>	<u>190</u>	<u>(18,517)</u>	<u>-</u>	<u>(19,956)</u>

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Thousands pesos of constant purchasing power as of December 31, 2007)

Guarantors' Combined Statements of Changes in Financial Position:

<u>For the year ended December 31, 2007</u>	<u>Icosa</u>	<u>Inmobiliaria</u>	<u>Servicios Axtel</u>	<u>Adjustments and Eliminations</u>	<u>Combined Guarantors</u>
Operating activities:					
Net income (loss)	Ps. 795	142	(32,208)	-	(31,271)
Non-cash items	<u>2,685</u>	<u>384</u>	<u>14,217</u>	<u>-</u>	<u>17,286</u>
Resources provided by (used in) operations	3,480	526	(17,991)	-	(13,985)
Net (investment in) financing from operations	<u>(4,741)</u>	<u>120</u>	<u>(1,089)</u>	<u>-</u>	<u>(5,710)</u>
Resources (used in) provided by operations, net	<u>(1,261)</u>	<u>646</u>	<u>(19,080)</u>	<u>-</u>	<u>(19,695)</u>
Financing activities:					
Increase in common stock	-	-	-	-	-
Loans payment, net	<u>-</u>	<u>(635)</u>	<u>-</u>	<u>-</u>	<u>(635)</u>
Resources provided by (used in) financing activities	<u>-</u>	<u>(635)</u>	<u>-</u>	<u>-</u>	<u>(635)</u>
Investing activities:					
Property, system and equipment, net	-	-	(3)	-	(3)
Other assets	<u>1,292</u>	<u>5</u>	<u>15,889</u>	<u>-</u>	<u>17,186</u>
Resources used in investing activities	<u>1,292</u>	<u>5</u>	<u>15,886</u>	<u>-</u>	<u>17,183</u>
Increase (decrease) in cash and equivalents	31	16	(3,194)	-	(3,147)
Cash and equivalents at the beginning of the year	<u>483</u>	<u>8</u>	<u>4,563</u>	<u>-</u>	<u>5,054</u>
Cash and equivalents at the end of the year	Ps. <u>514</u>	<u>24</u>	<u>1,369</u>	<u>-</u>	<u>1,907</u>

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Thousands pesos of constant purchasing power as of December 31, 2007)

<u>For the year ended December 31, 2006</u>	<u>Icosa</u>	<u>Inmobiliaria</u>	<u>Servicios Axtel</u>	<u>Adjustments and Eliminations</u>	<u>Combined Guarantors</u>
Operating activities:					
Net (loss) income	Ps. (1,066)	287	(6,024)	-	(4,671)
Non-cash items	<u>527</u>	<u>381</u>	<u>(1,003)</u>	<u>-</u>	<u>(95)</u>
Resources provided by (used in) operations	1,593	668	(7,027)	-	(4,766)
(Investment in) financing from operations, net	<u>(8,475)</u>	<u>(74)</u>	<u>(12,851)</u>	<u>-</u>	<u>(21,400)</u>
Resources (used in) provided by operations, net	<u>(6,882)</u>	<u>594</u>	<u>(19,878)</u>	<u>-</u>	<u>(26,166)</u>
Financing activities:					
Increase in common stock	6,800	-	17,639	-	24,439
Loans payments, net	<u>-</u>	<u>(470)</u>	<u>-</u>	<u>-</u>	<u>(470)</u>
Resources provided by (used in) financing activities	<u>6,800</u>	<u>(470)</u>	<u>17,639</u>	<u>-</u>	<u>23,969</u>
Investing activities:					
Property system and equipment, net	-	-	(24)	-	(24)
Other assets	<u>109</u>	<u>(128)</u>	<u>3,569</u>	<u>-</u>	<u>3,550</u>
Resources used in investing activities	<u>109</u>	<u>(128)</u>	<u>3,545</u>	<u>-</u>	<u>3,526</u>
Increase (decrease) in cash and equivalents	27	(4)	1,306	-	1,329
Cash and equivalents at the beginning of the year	<u>455</u>	<u>12</u>	<u>3,257</u>	<u>-</u>	<u>3,724</u>
Cash and equivalents at the end of the year	Ps. <u>482</u>	<u>8</u>	<u>4,563</u>	<u>-</u>	<u>5,053</u>

AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Thousands pesos of constant purchasing power as of December 31, 2007)

<u>For the year ended December 31, 2005</u>	<u>Icosa</u>	<u>Inmobiliaria</u>	<u>Servicios Axtel</u>	<u>Adjustments and Eliminations</u>	<u>Combined Guarantors</u>
Operating activities:					
Net (loss) income	Ps. (1,629)	190	(18,517)	-	(19,956)
Non-cash items	<u>799</u>	<u>420</u>	<u>3,986</u>	<u>-</u>	<u>5,205</u>
Resources (used in) provided by operations	(830)	610	(14,531)	-	(14,751)
Net (investment in) financing from operations, net	<u>(1,502)</u>	<u>94</u>	<u>7,008</u>	<u>-</u>	<u>5,600</u>
Resources (used in) provided by operations, net	<u>(2,332)</u>	<u>704</u>	<u>(7,523)</u>	<u>-</u>	<u>(9,151)</u>
Financing activities:					
Increase in common stock	3,039	-	25,589	-	28,628
Loans payment	<u>-</u>	<u>(706)</u>	<u>-</u>	<u>-</u>	<u>(706)</u>
Resources provided by (used in) financing activities	<u>3,039</u>	<u>(706)</u>	<u>25,589</u>	<u>-</u>	<u>27,922</u>
Investing activities:					
Property system and equipment, net	-	-	(51)	-	(51)
Other assets	<u>(908)</u>	<u>-</u>	<u>(16,330)</u>	<u>-</u>	<u>(17,238)</u>
Resources used in investing activities	<u>(908)</u>	<u>-</u>	<u>(16,381)</u>	<u>-</u>	<u>(17,289)</u>
(Decrease) increase in cash and equivalents	(201)	(2)	1,685	-	1,482
Cash and equivalents at the beginning of the year	<u>656</u>	<u>14</u>	<u>1,572</u>	<u>-</u>	<u>2,242</u>
Cash and equivalents at the end of the year	Ps. <u>455</u>	<u>12</u>	<u>3,257</u>	<u>-</u>	<u>3,724</u>

AXTEL, S.A. DE C.V. AND SUBSIDIARIES**Notes to the Consolidated Financial Statements**

(Thousand pesos of constant purchasing power as of December 31, 2007)

Guarantors – U.S. GAAP reconciliation of net income and stockholders' equity:

As discussed at the beginning of this note 24, the following reconciliation to U.S. GAAP does not eliminate the inflation adjustments for Mexican GAAP, since they represent an integral measurement of the effects of the changes in the price levels in the Mexican economy and, as such, are considered a more meaningful presentation than the financial reports based on historic costs for book purposes for Mexico and the United States.

The main differences between Mexican GAAP and U.S. GAAP and their effect on combined guarantors' net loss and stockholders' equity as of December 31, 2007, 2006 and 2005 is presented below, with an explanation of the adjustments.

		Year ended December 31,		
		2007	2006	2005
Net loss reported under Mexican GAAP	Ps	(31,271)	(4,671)	
				(19,956)
U.S. GAAP adjustments				
1. Deferred income taxes (A)		(7,092)	1,647	11,347
2. Allowance for post retirement benefits (B)		25,325	(5,875)	6,101
Total U.S. GAAP adjustments		18,233	(4,228)	17,448
Net loss under U.S. GAAP	Ps	(13,038)	(8,899)	(2,508)
		Year ended December 31,		
		2007	2006	
Total stockholders' equity reported under Mexican GAAP	Ps.	24,618	56,202	
U.S. GAAP adjustments				
1. Deferred income taxes (A)		(502)	6,876	
2. Allowance for post retirement benefits (B)		(1,793)	(24,557)	
Total U.S. GAAP adjustments		1,291	(17,681)	
Total stockholders' equity under U.S. GAAP	Ps.	25,909	38,521	

Guarantors-Notes to the U.S. GAAP reconciliation**A. Deferred income taxes**

Deferred income taxes adjustment in the stockholders' equity reconciliation to U.S. GAAP, as of December 31, 2007 and 2006, represented a decrease and increase of Ps. (502) and Ps. 6,876, respectively, as shown in the U.S. GAAP reconciliation.

AXTEL, S.A. DE C.V. AND SUBSIDIARIES**Notes to the Consolidated Financial Statements**

(Thousand pesos of constant purchasing power as of December 31, 2007)

B. Allowance for post retirement benefits

For the years ended December 31, 2004 and before, under Mexican GAAP (Bulletin D-3), severance payments were recognized in earnings in the period in which they were paid, unless such payments were used by an entity as a substitution of pension benefits, in which case, they were considered as a pension plan. Starting January 1, 2005, the new Bulletin D-3 replaces the issue of unforeseen payments with the one relating to "Payments Upon Termination of the Labor Relationship" and establishes certain valuation and disclosure requirements for those payments for reasons other than restructuring, which are the same as those for pension and seniority premium payments. Under U.S. GAAP, post-employment benefits for former or inactive employees, excluding retirement benefits, are accounted for under the provisions of SFAS 112, which requires recognition of certain benefits, including severance, over an employee's service life. For the years ended December 31, 2007, 2006 and 2005 the guarantors recorded a (decrease) increase in net income of Ps. 25,391, Ps. (5,875) and Ps. 6,101, respectively; and for 2006 the Company cancelled a deferred charge of Ps. 17,071, as recorded under Mexican GAAP. The US GAAP liability amounts to Ps. 44,608 and Ps. 31,489 as of December 31, 2007 and 2006, respectively.

Effective December 31, 2006, the Company adopted the recognition and disclosure provisions of FASB Statement No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans* (SFAS 158). SFAS 158 requires companies to recognize the funded status of defined benefit pension and other postretirement plans as a net asset or liability and to recognize changes in that funded status in the year in which the changes occur through other comprehensive income to the extent those changes are not included in the net periodic cost. The funded status reported on the balance sheet as of December 31, 2007 under SFAS 158 was measured as the difference between the fair value of plan assets and the benefit obligation on a plan-by-plan basis. The Company believes that the assumptions utilized in recording its obligations under its plans are reasonable based on its experience and market conditions. The incremental effect of applying SFAS 158 on the Company's financial position as of December 31, 2007 for items not yet recognized as a component of net periodic cost that were recognized in accumulated other comprehensive income was as follows:

		Before Application of SFAS 158	Adjustments	After Application of SFAS 158
Severance, seniority premiums and other post retirements benefits long term portion	Ps.	47,257	(2,649)	44,608
Deferred income taxes assets (noncurrent)		(13,232)	742	(12,490)
Total liabilities	Ps.	34,025	(1,907)	32,118

CERTIFICATION

I, Patricio Jimenez Barrera, certify that:

1. I have reviewed this annual report on Form 20-F of Axtel, S.A.B. de C.V.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;
4. The company's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the company and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (c) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal control over financial reporting.

Date: April 25, 2008

Axtel, S.A.B. de C.V.

/s/ Patricio Jimenez Barrera
Patricio Jimenez Barrera
Chief Financial Officer

CERTIFICATION

I, Tomas Milmo Santos, certify that:

1. I have reviewed this annual report on Form 20-F of Axtel, S.A.B. de C.V.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;
4. The company's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the company and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (c) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal control over financial reporting.

/s/ Tomas Milmo Santos
Tomas Milmo Santos
Chief Executive Officer

Date: April 25, 2008